

# California Real Estate Exam Prep Workbook

Sixth Edition

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CALIFORNIA REAL ESTATE EXAM PREP WORKBOOK SIXTH EDITION  
© 2021 Kaplan, Inc.

Published by DF Institute, Inc., d/b/a Kaplan Real Estate Education  
332 Front St. S., Suite 501  
La Crosse, WI 54601

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ISBN: 978-1-07-880839-2

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# PREFACE

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## REVIEW

The review reflects the current California real estate laws, rules, and regulations. Topics covered in the review are listed below.

### **Property ownership and land-use controls and regulations**

Topics include classes of property, property characteristics, encumbrances, types of ownership, descriptions of property, government rights in land, public controls, environmental hazards and regulations, private controls, water rights, and special categories of land.

### **Contracts**

Topics include general, listing agreements, buyer broker agreements, offers/purchase contracts, agreements, promissory notes/securities, purchase/lease options, and advance fees.

### **Financing**

Topics include general concepts, types of loans, sources of financing, how to deal with lenders, government programs, mortgages/deeds of trust/notes, financing/credit laws, loan brokerage, and types of loan originators.

### **Laws of agency and fiduciary duties**

Topics include law, definition and nature of agency relationships, types of agencies, and agents; creation of agency and agency agreements; responsibilities of agent to seller/buyer as principal; disclosure of agency; disclosure of acting as principal or other interest; termination of agency; and commission and fees.

### **Practice of real estate and disclosures (includes specialty areas)**

Topics include trust account management, fair housing laws, truth in advertising, recordkeeping requirements, agent supervision, permitted activities of unlicensed sales assistants, DRE jurisdiction and disciplinary actions, licensing, continuing education requirements and procedures, Consumer Recovery Account, general ethics, technology, property management/landlord-tenant rights, commercial/industrial/income properties, specialty areas, transfer disclosure statement, natural hazard disclosure statements, disclosure of material facts affecting property value, need for inspection and obtaining/verifying information, reports, and servicing diverse populations.

## **Property valuation and financial analysis**

Topics include value, methods of estimating value, and financial analysis.

## **Transfer of property**

Topics include title insurance, deeds, escrow, tax aspects, special processes, transfer through court supervision, and types of vesting.

# UNIT 1

## Property Ownership and Land-Use Controls and Regulations

### LEARNING OBJECTIVE

*When you have completed this unit, you will be able to accomplish the following.*

- ♣ Describe property ownership and land-use controls and regulations in California.

#### I. CLASSES OF PROPERTY/REAL ESTATE AND PERSONAL PROPERTY

##### A. Real estate

Real estate includes land plus improvements plus appurtenances, which include rights, privileges, and fixtures.

1. Land
2. Improvements

##### B. Personal property/chattel

1. Everything that is not real estate; movable items
2. Personal property—transferred by a bill of sale (real property—transferred by deed)

##### C. Personal property can become real property and vice versa

1. Personal property becomes real property by attachment.
2. Real property becomes personal property by severance.

## II. PROPERTY CHARACTERISTICS

### A. Physical characteristics of land

1. Immobile—The geographic location of a piece of land is fixed.
2. Unique or nonhomogeneous—All parcels differ geographically, and each parcel has its own location.

### B. Economic characteristics of land

1. Scarcity—Although there is a substantial amount of unused land, supply in a given location or of a specific quality can be limited.
2. Area preference or situs—These are people's choices and desires for a given area.

## III. LEGAL DESCRIPTIONS

### A. Methods of legal description

1. Metes and bounds—linear measurements, directions, and degrees
2. Rectangular survey/government survey—applies to over 30 states, especially in western United States
3. Recorded map (lot, block, subdivision)—urban/residential
4. Informal reference—street addresses are informal references that are not legal descriptions

### B. Survey

1. Lender may require
2. May reveal encroachments or compliance with setback requirements

## IV. TYPES OF OWNERSHIP—ESTATES AND ENCUMBRANCES

Both a tenant renting an apartment building and an owner of a house or condominium have estates in real property.

### A. Freehold estates

1. *Fee simple absolute* lasts forever and features the maximum control of use.
2. *Fee simple defeasible* lasts “so long as” the condition is not broken.
3. *Life estate* lasts for the duration of a person's lifetime.

### B. Less-than-freehold (leasehold) estates

1. Estate/tenancy for years—predetermined termination date; definite period. No notice is required.
  - a. Fixed term

- b. Ends automatically
- c. Advance notice

2. Periodic estate/tenancy—continues from period to period, such as month to month, until proper notice is given. It renews under the same conditions and terms upon payment of rent.

- a. Automatically renews

3. Estate/tenancy at will—continues at owner's consent. California has notice requirements.

4. Estate/tenancy at sufferance—when a “holdover tenant” stays beyond termination without consent. If a landlord accepts payments, it becomes a periodic tenancy.

5. The lessee has a leasehold estate; the lessor holds a leased fee estate and has a reversionary interest.

### **C. Encumbrances/imperfections**

These are nonpossessory interests in the lands of another. They may create a cloud on the title that might impair or lessen the owner's rights.

- 1. Easement—nonpossessory right to use the lands of another for a specific purpose
  - a. Appurtenant easement
  - b. Easement in gross
- 2. Deed restrictions/restrictive covenants/subdivision deed restrictions/condominium bylaws or covenants, conditions, and restrictions (CCRs)
- 3. Lien—claim that attaches to and is binding on property to secure debt repayment
- 4. Encroachment—unauthorized use of another person's land
- 5. License—revocable permission to use the land of another without creating an estate in land
- 6. Lis pendens—a recorded document that gives constructive notice of a pending lawsuit

## **V. TYPES OF OWNERSHIP**

The manner of holding title has significant legal and tax consequences. An attorney specializing in such matters should be consulted. Licensees should NEVER advise on how to take title.

### **A. Sole ownership/estate in severalty**

- 1. When property is owned solely and separately by one person or one entity, it is called an estate in severalty.
- 2. A corporation can hold title in severalty.

**B. Concurrent ownership**

1. Tenants in common—own undivided fractional shares with no right of survivorship. Each co-owner has equal right of possession.
2. Joint tenants—co-ownership with the right of survivorship
3. Community property
4. In trust—ownership in a fiduciary capacity for another
5. In partnership

**VI. SPECIAL CATEGORIES OF LAND****A. Condominium**

1. Real estate, portions of which are designated for separate ownership (units) and the remainder of which, including the physical structure, is designated for common ownership and use (common elements)
2. Fee simple interest in unit plus undivided interest in common elements as tenants in common transferred by deed
3. Each unit and its common element percentage is taxed, homesteaded, insured, and transferred as a separate parcel
4. Condominium conversion—the process of changing from rental apartments to condominium ownership

**B. Stock cooperative**

1. Ownership by a corporation, which in turn leases space to shareholders
2. Buyer receives corporate bylaws, shares of stock, and proprietary lease
3. Since there is no ownership of the unit, buyer does not receive a deed
4. Owner pays assessments/association fees

**C. Time-shares**

1. A common-interest ownership form where multiple owners have interest in a property
2. Each purchaser receives right to use the facilities for a certain period each year
3. Seven-day right of rescission

**D. Planned unit development (PUD)**

1. Consists of separately owned parcels of land together with membership in an association which owns common areas (e.g., a gated community)

2. Differs from a condominium in that the property owners actually own the land beneath the house, rather than the airspace of the condo unit

**(Note:** Present tenants of a proposed condominium, community apartment project, or stock cooperative must be given notice of the right to purchase their units for 90 days after the issuance of the public report.)

## VII. GOVERNMENT RIGHTS IN LAND

### A. Collect property taxes and special assessments

1. Ad valorem—according to value
2. May seize and sell by enforcing property tax lien
3. Special assessment—taxes levied against specific properties that benefit from a public improvement

### B. Eminent domain

1. Right to “take” private land for public use
2. Condemnation is the process
3. Fair compensation including property value plus damages

### C. Police power

1. Police power is enacting and enforcing laws governing land use to promote and support the public health, safety, morals, and general welfare.
2. Examples include zoning, building codes, subdivision regulations, and safety codes.
3. While zoning and so on may affect property value, it is generally not considered a “taking,” and requires no compensation.

### D. Escheat

1. Government’s reversionary right
2. Abandoned property or property of intestate owners with no heirs may revert to the government

## VIII. ZONING

### A. Typical zoning and land-use classifications

1. Residential, commercial, industrial/manufacturing, agricultural, mixed
2. Buffer zone is an area of land (e.g., a park) that separates two drastically different land-use zones

### B. Typical zoning controls and exceptions

1. Rezoning or amendment is a zoning change for an entire area.

2. Downzoning is a zoning change from dense to less dense usage.
3. Upzoning is a change from less dense to more dense usage.
4. Spot zoning is reclassification of a small area of land for use that does not conform to the zoning of the rest of the area.
5. Legal nonconforming use allows an owner to continue present use that no longer complies with current zoning (also called grandfathering).
6. Setback, side yard, and rear yard restrictions limit the location of improvements in relation to the position of the street.
7. Variance allows an individual owner to vary or deviate to prevent economic hardship.
8. Special (conditional) use (also called a special exception) is a specific type of variance allowing a different use.

## IX. BUILDING CODES

### A. Regulate building and construction standards

1. Designed to provide minimum standards
2. There are national and local standards—strictest standard prevails

### B. Building inspectors—responsible for enforcing building codes

1. Can make an exception when safety isn't compromised and standards not specifically violated

## X. ENVIRONMENTAL HAZARDS AND REGULATIONS

### A. Lead-based paint

1. Agent must give copy of U.S. Environmental Protection Agency (EPA) pamphlet to buyers and tenants of homes built before 1978
2. Buyers have 10-day opportunity to have home tested
3. Include warnings on purchase agreement and obtain signatures of buyers, sellers, and agents

### B. Radon gas

1. An odorless radioactive gas that enters through cracks in the basement and can cause lung cancer
2. EPA has determined what is an action level, but testing is not required
3. Measured in picocuries per liter of air (pCi/L)—Measured using an alphatrack detector or electret ion chamber detector

**C. Asbestos**

1. A material used for many years as insulation
2. Asbestos dust can be dangerous, even life threatening

**D. Groundwater contamination**

1. Comes from several sources
2. Most common are underground storage tanks, use of pesticides on farms, and waste disposal sites

**E. Environmental impact statement (EIS)**

1. A report that assesses the probable impact on the environment of a proposed project
2. Required of federal agencies in advance of major government actions (e.g., new highway or bridge construction)

**F. Superfund law**

1. Law involving liability for cleanup of sites affected by toxic materials
2. Anyone who touches the land can bear liability, even a tenant or a bank who gets property via foreclosure

**XI. SUBDIVISIONS****A. Subdivision Map Act**

1. Establishes procedures for filing a subdivision plan when property is divided into two or more parcels
2. Controls physical design aspects of a subdivision; ensures that areas devoted to public use, such as streets, will be properly improved initially

**B. Subdivision lands law**

1. Describes forms of ownership allowed in a subdivision of five or more parcels
2. Designed to prevent fraud and misrepresentation in selling of subdivisions
3. Public report

**C. Other subdivision requirements**

1. An environmental impact report (EIR) is required if a project will have a significant effect on the environment.
2. The Alquist-Priolo Earthquake Fault Zoning Act regulates development in earthquake zones.
3. The Street Improvement Act of 1911 authorizes local governing bodies to order street improvements (off-site improvements) and pay through a bond issue and special assessment.

**XII. WATER RIGHTS****A. Riparian rights**

1. Incidental to ownership of land abutting flowing water (stream, river, or watercourse)

**B. Littoral rights**

1. Incidental to ownership of land abutting water that is not flowing (lake, ocean, or sea arm)

**C. Other terms**

1. Accretion is the gradual addition to land through natural causes.
2. *Erosion* is the gradual loss of land through natural causes.
3. Avulsion is the sudden loss of land through natural causes.
4. *Accession* is an addition to property through the efforts of man or nature.

# UNIT 1 REVIEW QUESTIONS

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## True/False Questions

1. There are two classifications of property: real property and fixtures.
  - A. True
  - B. False
2. Real property is often described as a bundle of rights.
  - A. True
  - B. False
3. Land includes subsurface rights.
  - A. True
  - B. False
4. A fixture is not attached to land.
  - A. True
  - B. False
5. If trade fixtures or emblements are transferred, it will be by a deed.
  - A. True
  - B. False
6. Real property is movable.
  - A. True
  - B. False
7. Mineral rights refer to the right to remove substances from the land.
  - A. True
  - B. False
8. Air rights extend as high as can be reasonably used.
  - A. True
  - B. False
9. An example of an appurtenance is land bordering a river.
  - A. True
  - B. False
10. Personal property must be included in the purchase agreement to convey with the property.
  - A. True
  - B. False
11. An encumbrance is anything that has an effect on an owner's fee simple title to real estate or the use of the property.
  - A. True
  - B. False
12. An encumbrance can cloud the title to the property.
  - A. True
  - B. False
13. A deed restriction is an encumbrance that makes property the security for payment of a debt.
  - A. True
  - B. False
14. An appurtenant easement has a dominant tenement and a servient tenement.
  - A. True
  - B. False
15. Sole ownership is also called an estate in severalty.
  - A. True
  - B. False
16. Tenants in common must own equal shares.
  - A. True
  - B. False
17. In joint tenancy, the joint tenants do not benefit from the right of survivorship.
  - A. True
  - B. False
18. Community property is real or personal property acquired by a spouse during marriage.
  - A. True
  - B. False
19. A rectangular government survey land description starts at the point of beginning.
  - A. True
  - B. False
20. Metes-and-bounds measures are stated in a counterclockwise direction.
  - A. True
  - B. False

21. An acre contains 43,560 square feet.
  - A. True
  - B. False
22. The lot and block system is also called the subdivision system.
  - A. True
  - B. False
23. Planning, zoning, and building codes are examples of eminent domain.
  - A. True
  - B. False
24. The government exercises its power of eminent domain through a process called condemnation.
  - A. True
  - B. False
25. Property taxes are paid by the property owner to the federal government.
  - A. True
  - B. False
26. Escheat is the government's reversionary right when a property is abandoned.
  - A. True
  - B. False
27. Public controls are possible because of the government's escheat power.
  - A. True
  - B. False
28. Police power is the right of the government to enact and enforce laws governing land use.
  - A. True
  - B. False
29. Zoning is the division of a city into areas, or zones, limited to certain land uses, building requirements, or both.
  - A. True
  - B. False
30. Nonconfirming use limits the location of improvements in relation to the property lines.
  - A. True
  - B. False
31. Agents must give a copy of an Environmental Protection Agency pamphlet to buyers and tenants of homes built before 1978.
  - A. True
  - B. False
32. Radon gas is an odorless gas that is not radioactive.
  - A. True
  - B. False
33. Abatement, or removal, of asbestos can be performed by an unprofessional handyman.
  - A. True
  - B. False
34. An environmental impact statement is required of federal agencies in advance of major government actions, such as the construction of a new highway or bridge.
  - A. True
  - B. False
35. The penalty for noncompliance of a covenant is loss of title.
  - A. True
  - B. False
36. Deed restrictions run with the land and are binding on all present and future owners.
  - A. True
  - B. False
37. A common deed restriction used by homeowners associations are CC&Rs.
  - A. True
  - B. False
38. A deed restriction that prohibits property owners based on race is valid.
  - A. True
  - B. False
39. Littoral rights are incidental to land abutting flowing water.
  - A. True
  - B. False
40. An example of a body of water that falls under riparian rights is a river.
  - A. True
  - B. False
41. The property line of land that borders a navigable stream is the centerline of the waterway.
  - A. True
  - B. False
42. Owners of littoral rights have the right to make reasonable use of the water on their own property.
  - A. True
  - B. False

43. In condominium ownership, property owners own and finance their individual units.

- True
- False

44. A stock cooperative owner receives corporate bylaws, shares of stock, and a proprietary lease.

- True
- False

45. A time-share purchase has a three-day right of rescission.

- True
- False

46. A planned unit development differs from a condominium in that the property owners actually own the land beneath the house, rather than the airspace of the condo unit.

- True
- False

5. A plot plan

- shows contour of the land.
- shows the exterior of structures to be built.
- is used as an exact guide for construction of improvements.
- is used as a guide to the placement of structures and related improvements on the lot.

6. A roof that inclines from four sides is

- a hip roof.
- a gable roof.
- a trussed roof.
- a gambrel roof.

7. A developer who requested backfill would be using it for

- roadways.
- driveways.
- garden landscaping.
- replacing excavated earth against foundation walls.

### Multiple-Choice Questions

- The MOST common way for local planners to designate zoning for multiple residential units is
  - A-3.
  - C-3.
  - M-3.
  - R-3.
- An estate in real property consisting of an undivided interest in common in a portion of a parcel of real property, together with a separate interest in space in a residential, industrial, or commercial building, is a partial definition of
  - a condominium.
  - a planned development.
  - a community apartment.
  - a stock cooperative.
- Condominium projects are expected to grow in demand in the future primarily because of which factor?
  - Land value
  - Comfort of unit owners
  - Demand for sociability
  - Increased real property taxes
- A percolation test is used to determine
  - depth of footings.
  - quantity and potability of water.
  - capacity of soil to absorb water.
  - size of the cistern needed for a given building.
- Elevation sheets found in building plans refer to
  - an aerial view of the site.
  - pictures of the sides of the improvements as they will appear after completion.
  - topography of the land, indicating slope, the elevation of the sites, the streets, the sidewalks, and the curbs.
  - the interior of the house, framing, and itemization of the structure of the house.
- The distinguishing characteristic of real property, as opposed to personal property, is that real property
  - is immovable.
  - is a long-term asset.
  - has a high cost of acquisition.
  - can be depreciated over useful life.
- Personal property presents certain problems to a broker. It becomes difficult to ascertain its ownership because it can
  - become real property.
  - be alienated.
  - be hypothecated.
  - do all of these.
- Property is
  - real if tangible.
  - personal if a fixture.
  - personal if not real.
  - all of these.

12. Which criterion has the LEAST effect in determining whether an item is personal property?

- Time of annexation
- Manner of annexation
- Intention of the parties
- Relationship between the parties

13. A farm where a crop of corn was growing was sold. During the entire transaction, neither the buyer nor the seller discussed who was going to harvest the corn. The man who purchased the property assumed that the corn was his, but the seller had plans to harvest the crop at a later time. Under these circumstances,

- if the buyer wanted the corn, he should have specified this in the sales agreement.
- the corn is considered real property; therefore, the seller had no right to it.
- the seller has the right to harvest the corn because his intention is the controlling factor.
- the seller does not have a right to harvest the corn because he left the property, even though his intentions were there.

14. Which is considered real property?

- A stud in the wall of a house
- Fixtures removable by a tenant
- Fruit that was to be picked after the sale, as agreed upon by both the buyer and the seller
- Shrubs to be planted around a yard

15. Which notice is of importance in filing a mechanic's lien?

- Notice of Completion
- Notice of Nonresponsibility
- Notice of Cessation of Labor
- All of these

16. As defined by the real estate commissioner, all of the following can be blanket encumbrances EXCEPT

- trust deeds.
- mortgages.
- property taxes.
- mechanics' liens.

17. The right to the use and enjoyment of another's property short of an estate is an example of

- a deed.
- a leasehold.
- an easement.
- a subordination clause.

18. All of the following constitute a lien EXCEPT

- a license.
- a judgment.
- a mortgage.
- an attachment.

19. A judgment is an example of

- a voluntary general lien.
- an involuntary specific lien.
- a voluntary unspecific lien.
- an involuntary general lien.

20. If a Notice of Completion or a Notice of Cessation has not been recorded, all claimants have how many days after completion of the project to file a mechanic's lien?

- 30
- 60
- 90
- None of these

21. In new construction financing, the lender will usually release the final payment to the borrower when

- the work has been completed.
- the owner has accepted the property.
- the mechanic's lien period has expired.
- the notice of completion has been recorded.

22. A trustor must get the permission of the beneficiary when which of the following occurs?

- Boundary changes
- Restriction agreement
- Consolidation agreement
- All of these

23. Mortgages and deeds of trust differ in every respect EXCEPT

- title.
- security.
- parties.
- statute of limitations.

24. Which "runs with the land"?

- Covenants
- Appurtenant easements
- Stock in a mutual water company
- All of these

25. Mr. Able owned an unencumbered lot and decided to build. On May 2, the lumber company delivered \$1,000 worth of lumber to the property. On May 3, he obtained a construction loan for \$30,000 from People's Savings and Loan Association. The loan was recorded after the lumber was delivered. In June, more lumber was delivered and the completed structure was painted. In August, Mr. Able moved into the house. The lumber company could not collect its balance of \$2,000 and the painter could not collect \$4,000 for the painting. They each filed a mechanic's lien. If the property is sold at a foreclosure sale and nets \$30,000, the amount received by People's Savings and Loan would be

- \$24,000.
- \$29,000.
- \$30,000.
- nothing.

26. Davidson has an easement on Parkins's property. If Davidson is not a property owner, her easement is

- an easement in gross.
- a restrictive easement.
- an appurtenant easement.
- a nonpossessory encroachment.

27. Which is the BEST and most nearly complete definition of the term *encumbrance*?

- Any action taken relative to a property other than an acquisition
- Anything that affects or limits the fee simple title to property
- The use of property by a debtor to offer a creditor security for debt
- Degree, quantity, nature, and extent of interest a person has in property

28. A specified charge against real property that is used as security is defined as

- a lien.
- an easement.
- zoning and planning.
- subdivision restrictions.

29. The right to use and enjoy another's property short of an estate is an example of

- a deed.
- an easement.
- a leasehold.
- a subordination clause.

30. The words *ingress* and *egress* are related to

- utilities.
- fee title.
- streams.
- easements.

31. With respect to easements appurtenant, which statement is correct?

- An easement always gives the rights of ingress and egress.
- All encumbrances are liens, but all liens are not encumbrances.
- The dominant tenement is the land burdened and benefited by the easement.
- If the grantor conveys title to property, the easement passes automatically with the land.

32. A lease for a period of years that is held by the lessor is an example of

- real property.
- freehold estate.
- personal property.
- none of these.

33. In tenancy in common, there is ALWAYS a unity of

- possession.
- interest.
- title.
- time.

34. In real estate, the word *tenancy* means

- two or more people joined in an enterprise.
- a tenacious person.
- a device.
- a mode of holding ownership by a tenant or title holder.

35. Under common law, it is necessary to give notice to terminate

- tenancy for years.
- tenancy at sufferance.
- tenancy at will.
- none of these.

36. Involuntary alienation of an estate means

- the estate cannot be transferred without the consent of the owner.
- ownership of estates may be transferred by operation of law.
- aliens are forbidden to own estates in fee simple in California.
- no one can be compelled to transfer title without giving consent.

37. A document deposited with the county recorder to indicate pending litigation is

- a promissory note.
- a trust deed.
- a lis pendens.
- a pending deed.

38. Which would cause an owner of a fee simple estate to convert her interest to a less-than-freehold estate?

- Granting oil and mineral rights to a third party
- A sale-leaseback
- Leasing for the purpose of agricultural use for a period of five years
- Both granting oil and mineral rights to a third party and leasing for the purpose of agricultural use for a period of five years

39. In real estate, the word *tenancy* means

- a method or mode of holding title.
- two or more people joined in an enterprise.
- a tenacious person.
- a device.

40. Three persons hold undivided interests in real property as tenants in common. This MOST likely means that they

- hold equal shares.
- hold unequal shares.
- took title at the same time.
- cannot locate their particular interests in the property.

41. Which type of estate represents the greatest interest a person can have in real property?

- Easement
- Fee simple estate
- Life estate
- Less-than-freehold estate

42. Which form of ownership consists of an undivided interest with the right of survivorship?

- Life estate
- Severalty
- Joint tenancy
- Tenancy in common

43. Co-ownership of property with undivided interests without the right of survivorship would be

- life estate.
- joint tenancy.
- severalty.
- tenancy in common.

44. Which would be the BEST description of a fee simple absolute estate?

- Greatest interest held in land
- Estate of inheritance
- Owning property
- Estate for years

45. A joint tenancy can be created by deeds conveying undivided interests by

- transfer from a wife deeding her separate property to herself and husband as joint tenants.
- transfer to executors of an estate as joint tenants.
- transfer from tenants in common deeding to themselves as joint tenants.
- all of these.

46. Which area is the largest?

- Two sections
- 10% of a township
- Four square miles
- 5,280 ft.  $\times$  10,560 ft.

47. A commercial acre is BEST defined as

- any parcel of 43,560 sq. ft.
- any acre located outside of "R" zoning.
- an acre zoned for commercial purposes.
- an acre after deductions for streets and alleys.

48. "Beginning at a point on the southerly line of O Street, 150 feet westerly of the SW corner of the intersection of O and 8th Streets; running thence due south 300 feet to the northerly line of P Street, thence westerly along the northerly line of P Street, 100 feet; thence northerly and parallel to the first course, 300 feet, to the southerly line of O Street; thence easterly along the southerly line of O Street, 100 feet, to the point or place of beginning." This is an example of

- a U.S. government survey.
- a U.S. geodetic survey.
- a metes-and-bounds description.
- a lot, block, and tract description.

49. Whatever the purpose of a land survey, the resultant description should contain

- a definite point of beginning and definite parcel corners.
- a specific length and direction of the sides of the property.
- the area in accepted units of measure contained within the described boundaries.
- all of these.

50. The state fiscal year falls between

- January 1 and December 31.
- June 30 and July 1.
- July 1 and June 30 at midnight.
- December 31 and January 1 at midnight.

51. Which entity has the responsibility for determining property values for real property tax purposes?

- Assessor's office
- Tax commissioner
- Board of equalization
- Board of supervisors

52. Eminent domain does NOT apply to

- a zoning authority changing the use and therefore the value of the property.
- just compensation for the fair market value of the property.
- the right of the government to take property.
- condemnation proceedings.

53. Police power may be defined as the right or power of regulation by government for the promotion of the health, safety, or general welfare of the public. Which of the following is an example of the exercise of police power?

- Condemnation of property by the federal government
- Zoning by a municipality
- Restrictions in a deed
- The taking of private property for use by a municipality

54. The courts have upheld a government's authority to enact laws for the health, welfare, safety, and morals of the general public under the doctrine of police power. All of the following are proper exercises of police power EXCEPT

- building ordinances and permits.
- land-use planning and zoning.
- right of taxation.
- the establishment of rent control.

55. Police power may be defined as a regulation by government for the promotion of the health, safety, or general welfare of the public. Which of the following is an example of the exercise of police power?

- The taking of private property for use by a municipality
- Condemnation of property by the federal government
- Zoning by a municipality
- Restrictions in a deed

56. The primary justification for zoning ordinances is that they

- promote conformity in the outward appearance of structures.
- promote the general health, safety, and welfare of the community.
- limit the supply of specific businesses within a zoned area.
- increase the tax base of the local governing body.

57. The California sales tax applies to

- real and personal property.
- tangible personal property.
- ad valorem taxation.
- all of these.

58. A commercial property no longer has a conforming use because it exists in an area where the zoning has been changed. The owner of this property has suffered a hardship because of the zoning change. What could the owner obtain as an exception to this new zoning that would be a benefit to him?

- Spot zoning
- A conditional use permit
- A variance
- Any of these

59. The second installment of real property taxes would become due and delinquent on which date?

- February 1 and April 10
- November 1 and February 1
- December 10 and February 1
- December 10 and April 10

60. On or before June 30 each year, property for which owners are delinquent in their taxes is declared in default. This date is important because

- the power of sale on or before June 30 starts the five-year period of redemption.
- the occupant of the property must vacate the premises within 90 days.
- interest on the delinquent taxes will begin from December 10.
- all of these are true.

61. In ridding an area of nonconforming uses, rezoning ordinances may require that certain conditions be met. These would include all of these EXCEPT

- prohibition of rebuilding.
- prohibition of expansion.
- retroactive zoning ordinances.
- allowing a reasonable time (amortized period) within which the abuses may be eliminated.

62. When a railroad needs specific land and the owner objects, the railroad may exercise the right of

- caveat emptor.
- eminent domain.
- injunction.
- writ of replevin.

63. A zoning designation that allowed multiple dwellings was changed. What effect would this have on an existing apartment building in the area?

- It would be in violation of the zoning law.
- It would be violation of the zoning law with regard to municipal and local ordinances.
- It would be a nonconforming use.
- It would be a variance.

64. *Escheat* is a legal term meaning

- that a fraud has been committed.
- an agent's license has been revoked.
- property under a trust deed may be reconveyed.
- property has reverted to the state.

65. Which lien would MOST likely have had priority?

- A public improvement assessment created on April 15, 2004
- A trust deed executed on March 27, 1998, and recorded on March 29, 2004
- A trust deed executed and recorded on March 28, 2004
- A mechanic's lien resulting from work started on March 27, 2004

66. The Subdivision Map Act

- is administered by the real estate commissioner.
- requires a subdivider to secure a public report.
- requires a subdivider to file a subdivision map with the State Department of Real Estate.
- is regulated by city and county planning commissions and allows them to standardize the regulations that govern subdivisions.

67. The Alcoholic Beverage Control Act prohibits the issuance of an on-sale general license to

- a club that has been in existence for less than six months.
- a hotel that has been operating for less than six months.
- a cafeteria that has been in operation for less than nine months.
- a restaurant that has been in operation for less than one year.

68. The California Franchise Investment Law protects

- the public on a fair, just, and equitable basis.
- only a franchisor who has a net worth of \$5,000.
- new franchisees contemplating the purchase of a franchise.
- the purchaser of a franchise who is from out of state.

69. An owner of a five-unit apartment complex intends to sell each unit to different individuals. He wants each to own an estate in each unit with ownership of structures and land in joint ownership. Under these circumstances, this plan would be considered

- a partition.
- a subdivision.
- lot-splitting.
- a variance.

70. What would be included in local building codes?

- The establishment of building materials that may be used and the costs of materials
- Architectural design of buildings, as well as size and height
- Protecting the health and safety of the city
- All of these

71. State-enabling legislation gives cities and counties various controls over real property. The enabling legislation gives to cities and counties all but

- lien and attachment laws.
- subdivision and land-use regulations.
- local planning and zoning ordinances.
- rent control and city codes.

72. Construction on a single-family residence started on January 20, 1978. The owner knows that a portion of the interior of the home was painted using lead-based paint. A prospective buyer discusses the plan to demolish and rebuild the home with the owner. What, if any, are the owner's disclosure obligations regarding the lead-based paint?

- Because the construction of the dwelling began after 1978, no disclosure needs to be made.
- Because the prospective buyer plans on demolishing the entire dwelling, no lead-based paint disclosure needs to be made.
- Actual knowledge of lead-based paint for a one-to-four-unit residential dwelling must be disclosed.
- Target housing for lead-based paint need only be made for dwellings constructed after 1978.

73. Radon gas is a naturally occurring radioactive gas. Radon gas is odorless and invisible, and it may result in cancer. This gas can't be seen, smelled, or tasted. It results from the decay of radioactive elements found naturally in soil. It moves, without any intervention from people, up through cracks in foundations and floors. Radon gas is considered

- a natural hazard.
- an environmental hazard.
- an unmitigable hazard.
- a hazard requiring a percolation test.

74. Which of the following would constitute a legitimate and lawful use of a deed restriction?

- That the property "could be used only for education or religious purposes"
- That the property "cannot be conveyed for 10 years"
- That the property "could be conveyed only to a Caucasian"
- That the property "could be sold only for more than one dollar"

75. Which statement is TRUE?

- A condition precedent runs with the land.
- A condition precedent is an involuntary servitude.
- A condition precedent takes the form of a covenant.
- None of these.

76. The personal, revocable, and unassignable permission or authority to do one or more acts on the land of another without possessing any interest therein is the definition of

- easement.
- encroachment.
- license.
- option.

77. Which would be LEAST likely to make the title of real property unmarketable?

- Public restrictions under zoning ordinances and building codes
- Private restrictions in a deed
- Cloud on title through adverse possession of the property
- A lis pendens filed by the wife of the owner

78. Appurtenant riparian rights refer to land that abuts

- watercourses.
- streams.
- rivers.
- all of these.

79. The act of a nonriparian owner who diverts water from a nearby lake or river for personal beneficial use is known as

- accretion.
- prescription.
- percolation.
- appropriation.

80. Matthew Schmidt and Angela Schmidt, a married couple, attended a time-share presentation at a hotel in San Diego County, California. The time-share development was located in Lassen County, California. In addition to a complementary dinner and an entertaining presentation, the time-share developers gave all attendees complementary passes to stay the night at the hotel. Upon awakening the next morning, the Schmidts realized they both regretted the purchase of a time-share. Which of the following statements accurately describes the Schmidts' situation as it pertains to the time-share purchase?

- A. The Schmidts may cancel the purchase, if done within seven weeks.
- B. The Schmidts may cancel the purchase, if done within seven calendar days.
- C. Because the presentation was in San Diego County, but the time-share development is located in Lassen County, the Schmidts will not be able to get a refund.
- D. The Schmidts are contractually bound by the terms of the time-share purchase agreement.

81. Latoya Williams purchased a \$3-million-dollar residential condominium unit located on the fifth floor of the complex. Williams put 20% down and took out a 30-year fixed mortgage for the rest of the purchase price. William's condo has three bedrooms, two bathrooms, and an open floor plan. Outside the family room is a balcony only Williams can access. Part of the purchase price also included two assigned parking spaces in the parking structure and an assigned storage unit in the apartment's basement. Excluding the common elements, what does Williams, and Williams alone, own?

- A. The airspace within the condo unit and the balcony
- B. The condo, surface rights to the land, air rights above the condo
- C. The airspace within the condo unit
- D. Nothing by herself—entire condominium belongs to the tenants association

# UNIT 2

## Contracts

### LEARNING OBJECTIVE

*When you have completed this unit, you will be able to accomplish the following.*

- ♣ Describe real estate contracts in California.

#### I. CONTRACT BASICS

##### A. Definition of a contract

1. An agreement between two or more parties to do or not to do a specific thing

##### B. Conditions of a contract

1. A valid contract contains all essential elements.
2. A voidable contract appears to be valid, but one party may disaffirm because, for example, that party was subject to duress, undue influence, fraud, or misrepresentation.
3. A void contract is not enforceable because it does not contain all essential elements.

##### C. Enforceable vs. unenforceable

1. In addition to being valid, void, or voidable, a contract can be enforceable or unenforceable.
2. A void contract is, by definition, unenforceable. A voidable contract is enforceable only by the injured party.
3. Valid contracts meet all essential elements but can be unenforceable by the courts (e.g., certain oral contracts, statute of limitations has expired, laches [not enforced in timely manner]).

**D. Parties to a transaction; -or vs. -ee****II. PERFORMANCE AND DISCHARGE OF OBLIGATIONS****A. Unilateral vs. bilateral**

1. Unilateral—promise exchanged for performance
2. Bilateral—promise exchanged for a promise

**B. Executed vs. executory**

1. Executed—duties completed by both parties; performed
2. Executory—one or both parties need to complete part of the contract; yet to be fully performed

**C. Amendments**

1. Changes or modifications to a contract must be in writing and signed by all parties

**D. Addendum**

1. Additional material attached to and made part of the initial agreement document

**E. Statute of limitations**

1. Two years for oral contracts
2. Four years for written contracts
3. Doctrine of laches—used by courts to deny a claim because of undue delay in assertion

**III. ESSENTIAL ELEMENTS OF A VALID CONTRACT**

- Consent
- Capacity
- Consideration
- Lawful object

**IV. STATUTE OF FRAUDS****A. Agreement in writing**

1. Statute of frauds requires that certain contracts be in writing to be enforceable
2. Includes contracts for the transfer of title to real estate but NOT leases of 12 months or less

**B. Agreement signed**

1. Both spouses must sign a deed to sell community property or release homestead rights.
2. Only one spouse may sign a listing agreement for it to be enforceable against both spouses on community property.
3. Only the grantor, not the grantee, is required to sign a deed for it to be valid.

**V. TYPES OF REAL ESTATE CONTRACTS****A. Purchase agreement/offer to purchase/contract of sale**

1. Bilateral/promise for a promise
2. Offer becomes a valid and binding contract when acceptance is communicated
3. Executory until performance by parties (closing)
4. May include contingency clause allowing buyer to terminate under certain conditions
5. “Time is of the essence” clause requires performance within time specified
6. Earnest money not required to create valid purchase agreement

**B. Option**

1. Owner (optionor) sells right to purchase to prospective buyer (optionee) at a fixed price for a designated period
2. Option fee paid by optionee for the right
3. Optionor retains option fee if no performance by optionee
4. Unilateral contract; becomes bilateral when option exercised by optionee

**C. Lease**

1. Elements of a lease
2. Lessor (landlord) gives right to occupy to lessee and has reversionary interest to retake possession
3. Lessee (tenant) may transfer rights
  - a. Sublease
  - b. Assignment
  - c. Unless a lease expressly prohibits it, a tenant can assign or sublease the interest in the property to a third party without landlord's consent
4. Types of leases

5. Constructive eviction—a tenant may vacate and be released of all further obligations if lessor does not meet obligations
6. A lease may be terminated by mutual agreement; called a surrender

## **VI. REMEDIES FOR BREACH OF CONTRACT/DEFAULT**

### **A. Mutual rescission**

1. Mutual cancellation of obligations and return of all parties to their original condition before the contract was executed

### **B. Action for damages**

1. Suit for monetary damages
2. Accept liquidated damages

### **C. Specific performance**

1. An action to force another party to buy or sell according to a contract

# UNIT 2 REVIEW QUESTIONS

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## True/False Questions

1. A contract is an agreement between two or more parties to do something or to refrain from doing something.
  - A. True
  - B. False
2. A valid contract contains only one legal requirement.
  - A. True
  - B. False
3. A party who does not fulfill the promise made in a contract is in default.
  - A. True
  - B. False
4. A contract is said to be an executory contract when all obligations have been completed.
  - A. True
  - B. False
5. In a bilateral contract, only one party promises to do something or to refrain from doing something.
  - A. True
  - B. False
6. In an open listing, the brokerage only gets paid if the broker is the procuring cause.
  - A. True
  - B. False
7. With an exclusive agency, the brokerage gets paid if the property sells, unless the seller finds the buyer.
  - A. True
  - B. False
8. With an exclusive right-to-sell listing, the broker is entitled to a commission no matter who sells the property, even if the owner sells the property.
  - A. True
  - B. False
9. A net listing is ethical and legal and is encouraged.
  - A. True
  - B. False
10. In a buyer-broker agreement, the seller is the principal.
  - A. True
  - B. False
11. A buyer-broker agreement can only be an exclusive right to buy.
  - A. True
  - B. False
12. With a buyer-broker agreement, the buyer can purchase a property through any source.
  - A. True
  - B. False
13. The buyer-broker agreement specifies the type of property the buyer is seeking.
  - A. True
  - B. False
14. The buyer-broker agreement provides for the buyer's acceptance of the broker's representation of other buyers seeking the same or similar properties.
  - A. True
  - B. False
15. A purchase contract is a unilateral contract.
  - A. True
  - B. False
16. The offer becomes a valid and binding contract when acceptance is communicated.
  - A. True
  - B. False
17. The purchase contract is executory until performance by both parties.
  - A. True
  - B. False

18. Contingency clauses in the purchase contract allow the buyer to terminate the contract under certain conditions.

- True
- False

19. Statute of frauds requires all contracts to be in writing.

- True
- False

20. The statute of limitations states that legal action must be brought within two years of an oral contract.

- True
- False

21. An addendum is used to make changes or modifications to a contract.

- True
- False

22. A unilateral agreement is binding from the beginning.

- True
- False

23. Both spouses must sign to sell community property.

- True
- False

24. A real estate loan only requires one instrument, the promissory note.

- True
- False

25. The promissory note is used to identify the real estate that serves as assurance.

- True
- False

26. The promissory note is the evidence of the debt.

- True
- False

27. A promissory note creates a lien on property.

- True
- False

28. An option is a bilateral agreement.

- True
- False

29. A lease option, unlike an option alone, conveys the right of possession as well as the option right.

- True
- False

30. The right of first refusal is the right of a person to have the opportunity to purchase or lease real property.

- True
- False

31. In a sale-leaseback, the owner sells the property to an investor who leases it back.

- True
- False

32. In a lease agreement, the tenant is the lessor.

- True
- False

33. There is a separate license available to operate a prepaid rental listing service (PRLS).

- True
- False

34. Licensed real estate brokers are exempt from this requirement.

- True
- False

35. Licensees must provide a prospective tenant with a DRE-approved written contract.

- True
- False

36. If the licensee fails to provide a list of at least five rental properties to the prospective tenant within five days, the advance fee must be refunded in full.

- True
- False

### Multiple-Choice Questions

- An executory contract is
  - a written contract that cannot be altered by oral agreement.
  - a contract that is yet to be performed by one or both parties.
  - a contract with an executor of an estate.
  - a contract that has been fully performed.

2. An executed contract is a contract
  - A. under the jurisdiction of the probate court.
  - B. signed, notarized, and recorded.
  - C. completed and fully performed by both parties.
  - D. to be rewritten.
3. A fire insurance policy can be canceled by the insurance company
  - A. if the company gives the insured notice within a reasonable time before cancellation.
  - B. at any time without notice.
  - C. without notice if the buyer has had excessive losses.
  - D. only after the company has given written notice and the insured has signed an acceptance.
4. Taylor, Hughes, and Kent each own a one-third undivided interest as tenants in common in a 640-acre farm. Hughes leases his interest to Jones for five years without the knowledge and consent of Taylor and Kent. In these circumstances, all of these statements are correct EXCEPT
  - A. Hughes could lease his one-third interest without the consent of Taylor and Kent.
  - B. the lease is invalid between cotenant-lessee and cotenant-lessor.
  - C. the lease is valid between cotenant-lessee and cotenant-lessor.
  - D. the lessee has an equal right of possession of the entire farm with the other cotenants.
5. The terms *good*, *sufficient*, *valuable*, and *adequate* relate to
  - A. performance.
  - B. value.
  - C. consideration.
  - D. all of these.
6. A contract that is NOT yet fully performed is
  - A. voidable.
  - B. executed.
  - C. executory.
  - D. unenforceable.
7. A tenant agrees to a commercial lease from a landlord. The landlord has an attorney draw up the lease agreement. What are the requisites for a valid lease?
  - A. The words "let and demise" to make the lease legal
  - B. The signature of the lessee in possession and already paying rent
  - C. The term, consideration, and description of the property
  - D. All of these
8. For a real estate sales contract to be recorded, it must
  - A. contain a granting clause.
  - B. be signed and acknowledged by seller and buyer.
  - C. be signed and acknowledged by seller.
  - D. be signed and acknowledged by buyer.
9. When an existing contract is replaced by an entirely new contract, this is an act of
  - A. novation.
  - B. subrogation.
  - C. rescission.
  - D. hypothecation.
10. A contract signed under duress would be
  - A. void.
  - B. voidable.
  - C. unenforceable.
  - D. illegal.
11. Certain contracts to be held enforceable in court under the statute of frauds must be in writing. Which of these would be required to be in writing?
  - A. Employment of a real estate broker to sell stock-in-trade and goodwill of a business
  - B. Employment of a real estate broker to find a business to purchase
  - C. Employment of a real estate broker to negotiate one-year leases on business property
  - D. Any agreement not to be performed within one year
12. *Rescind* MOST nearly means
  - A. terminate.
  - B. rewrite.
  - C. annul.
  - D. reject.

13. The legal term *laches* is BEST described as
  - A. a writ of attachment.
  - B. a deficiency judgment.
  - C. a court with no jurisdiction.
  - D. inexcusable delay in asserting a legal right.
14. Which word is MOST closely associated with the term *rider*?
  - A. Accretion
  - B. Amendment
  - C. Person
  - D. Lien
15. A voidable contract is
  - A. unenforceable.
  - B. illegal.
  - C. enforceable.
  - D. valid until some action is taken to void it.
16. Broker Wilson did not present a second offer on a particular property but rather held it as a backup offer while the seller was considering the first offer. This is
  - A. permissible.
  - B. not permissible because an agent should present all offers.
  - C. not permissible because the second offer should be returned so the offeror can make a larger offer.
  - D. not permissible because the second offer should be returned so the offeror might look at other property.
17. A listing agreement in which the owner promises to pay a commission under all circumstances of sale, except if she sells the property herself, is known as
  - A. an exclusive agency listing.
  - B. an exclusive right-to-sell listing.
  - C. a net listing.
  - D. none of these.
18. A broker used the following phraseology in his listing contract: "In consideration of the execution of the foregoing, the undersigned broker agrees to use diligence in procuring a purchaser." This is BEST described as
  - A. superfluous in such contracts.
  - B. a necessary item in the creation of a unilateral contract.
  - C. a necessary element in the creation of a bilateral contract.
  - D. an agreement to advertise the property.
19. A final, specific, and definite termination date is required by law on all agreements between seller and real estate agent EXCEPT
  - A. a written instrument giving one agent the right to sell property for a specified time but reserving the right of the owner to sell the property himself without paying a commission.
  - B. a written agreement between owner and agent giving the agent the right to collect a commission if the property is sold by anyone during the term of his agreement.
  - C. a written authorization given by a property owner to a real estate agent wherein said agent is given the right along with other brokers to secure a purchaser.
  - D. an agreement in writing wherein it is provided that an agent appointed in an exclusive capacity may retain as compensation for his services all sums received over and above a net price to the owner.
20. Jones signed a listing agreement with Brown, a broker, stating that he would pay 6% commission to Brown upon the sale of his house. Brown promised to use diligence in attempting to find a buyer. This contract is
  - A. unilateral executory.
  - B. unilateral executed.
  - C. bilateral executed.
  - D. bilateral executory.
21. The MOST common listing agreement allows the broker to
  - A. find a purchaser, obtain an offer, and bind the principal to that offer.
  - B. find a purchaser, fill out the deposit receipt, obtain an offer, and present the offer.
  - C. guarantee the purchaser will accept.
  - D. convey title.
22. Assuming that a broker convinced a seller that it would take a lot of work to sell his house, the seller agreed to pay a 14% commission. This would be a violation of
  - A. Civil Code.
  - B. usury law.
  - C. real estate law.
  - D. none of these.

23. Javier Salazar, a broker, worked with a buyer without a written buyer-broker representation agreement. After searching through the multiple listing service (MLS), Salazar found a property that suited the buyer's needs. Salazar advised the buyer carefully, not only with the offer, but with many other aspects of the purchase transaction. The offer was accepted and, several months later, escrow closed on the property. Salazar was not paid. Which of the following parties will Salazar MOST likely sue for his portion of the commission?

- A. The selling agent
- B. The seller
- C. The listing agent
- D. The buyer

24. John Lee entered into a written exclusive right-to-buy buyer-broker representation agreement with a real estate broker. During the term of this buyer-broker agreement, Lee found—by himself—a property that suited his needs. All of the following statements are incorrect, EXCEPT

- A. with this type of buyer-broker agreement, Lee will always pay his broker's commission.
- B. Lee's duty to pay the commission will be extinguished if his broker accepts a commission from the seller or the seller's agent.
- C. because Lee found his own property, Lee will not have to pay his broker's commission.
- D. this type of buyer-broker agreement is illegal in California.

25. Assume that after the seller accepted an offer, the broker gave a copy of the signed acceptance to the buyer. The liquidated damages clause was not initialed by seller or buyer. Later, the buyer informed the broker that he did not want to buy the property, was canceling his contract, and demanded the return of his deposit. If the seller and the broker refuse,

- A. the buyer has the right to rescind the contract anytime before close of escrow.
- B. the broker may keep half the deposit and return the balance to the buyer.
- C. the broker must return the deposit but can sue the seller for commission.
- D. the contract is enforceable and the buyer may be subject to damages or a suit for specific performance.

26. A broker had a listing on a property on which a buyer placed a deposit. Seller and buyer signed a deposit receipt. Before the transaction was consummated, the buyer approached the broker and asked if she could paint the inside of the house. In these circumstances,

- A. the broker may give permission for the buyer to paint.
- B. the broker could allow buyer to enter and make repairs provided the buyer pays rent.
- C. the broker must get written permission from the seller.
- D. a written agreement must be signed between the buyer and the broker on the amount and extent of repairs to be authorized.

27. Williams buys a lot in a subdivision of 30 lots. He signs a sales agreement with a provision that he will not put up a For Sale sign on his lot until the subdivider sells all the remaining lots. Williams may

- A. not put up a sign because of the agreement he signed.
- B. not put up a sign because the subdivider will hold him civilly liable.
- C. put up a sign of any dimensions because such an agreement is a restraint of trade.
- D. put up a sign of reasonable size because such agreements have been declared void by law.

28. The buyer would not give a \$1,000 check to the broker until the seller accepted the offer. What phrase do you think the broker should include in the deposit receipt to satisfy the buyer's request?

- A. Buyer to deposit a \$1,000 check with broker upon acceptance of offer by buyer
- B. Broker to collect \$1,000 from buyer on seller's acceptance
- C. No contract exists because of lack of consideration
- D. Buyer agrees to deposit \$1,000 cash with broker immediately upon seller's acceptance of buyer's offer

29. An offer is terminated by

- A. revocation by the offeror.
- B. revocation by the offeree.
- C. rejection by the offeror.
- D. a change in the offer made by the offeror.

30. A prospective buyer pays \$2,000 for a four-month option to purchase a \$300,000 property. All of these statements are true EXCEPT

- a unilateral contract has been established.
- the optionor's temporary surrender of the right to sell is valuable consideration.
- the optionee has acquired a legal interest in the property.
- the agreement imposes no obligation on the optionee to purchase the property.

31. Because land is unique in character and often cannot be substituted for another parcel, the courts have made available the right to request specific performance. What person would LEAST likely request such an action?

- The seller of a large tract of land
- The seller of a single-family residence
- The buyer of a single-family residence
- A broker acting as an agent of the seller

32. The written employment agreement, required by the Commissioner's regulations, between an employing broker and a salesperson is an example of

- implied contract.
- ratification.
- unilateral contract.
- bilateral executory contract.

33. Which document does NOT qualify for recording?

- A notice of completion
- A conditional sales contract
- A trustee's deed
- A promissory note secured by a deed of trust

34. What statement must be specifically stated in a purchase option agreement?

- A statement that the optionee has the right to purchase the subject property and a statement to the effect that the optionor can retain the price paid for the option
- A statement to the effect that the agreement is irrevocable
- A statement that the optionee has the right to purchase the subject property
- A statement to the effect that the optionor can retain the price paid for the option

35. A prospective buyer pays \$200 for a four-month option to purchase a \$30,000 property. All of the following are true EXCEPT

- a unilateral contract has been established.
- the optionor's temporary surrender of the right to sell is valuable consideration.
- the optionee has acquired a legal interest in the property.
- the agreement imposes no obligation on the optionee to purchase the property.

36. Are either or both of the following parties allowed to collect an advance fee for loan modification or loan forbearance work?

- Attorneys-at-law
- Real estate brokers
- Both of these
- Neither of these

# UNIT 3

## Financing

### LEARNING OBJECTIVE

*When you have completed this unit, you will be able to accomplish the following.*

- ♣ Describe real estate financing in California.

#### I. FINANCING INSTRUMENTS

##### A. Promissory note

1. Evidence of a debt
2. Secured by mortgage or trust deed
3. A negotiable instrument considered personal property; cannot be recorded

##### B. Mortgage and deed of trust

1. Security instruments
2. Include covenants—causes of foreclosure

##### C. Mortgage

1. Two-party instrument
2. Borrower = mortgagor; lender = mortgagee
3. Most common financing instrument in United States; California, however, favors deed of trust

**D. Deed of trust/trust deed**

1. Three-party instrument
2. Borrower = trustor; lender = beneficiary; third party = trustee
3. Property is conveyed by borrower to a third party (trustee) as security for loan
4. Trustee holds naked (bare legal) title on behalf of the lender (beneficiary)
5. Borrower (trustor) holds equitable title, and deed of trust is a lien
6. Trustee has authority, in case of default, to conduct foreclosure process, sell the property, and sign a deed

**E. Satisfaction**

1. When a mortgage note is paid, the mortgagee records the satisfaction to release the lien.
2. When a trust deed note is paid, the trustee records the deed of reconveyance to release the lien. (Do NOT confuse this with a trustee's deed, which is used in the event of foreclosure.)

**F. Assumption vs. subject to**

1. If a buyer purchases property "subject to" a mortgage, the seller remains liable.
2. If a buyer assumes a loan, the buyer becomes primarily liable for the debt and the original borrower retains secondary liability unless the lender releases the original borrower from liability.
3. There are no loan origination fees or points when a borrower assumes or purchases subject to a mortgage.

**G. Land contract/real property sales contract/installment contract/contract for deed**

1. Form of owner financing and security arrangement
2. Seller (vendor) keeps legal title; buyer (vendee) has equitable title, takes possession, and makes payments, receiving deed when payments are complete
3. Process used for CalVet loans, where Department of Veterans Affairs (VA) purchases property and sells to veteran under a land contract
4. Vendor must use payments from vendee to make any existing loan payments before using it for another purpose

## II. FORECLOSURE

Foreclosure is a legal procedure whereby property used as security for a debt is taken by a creditor or sold to pay off the debt.

### A. Judicial foreclosure/equitable action (for mortgages)

1. A lawsuit is brought by a mortgagee in superior court to obtain a court order to sell.
2. The property is sold by the sheriff to the high bidder at a public sale.
3. If the sale proceeds exceed the cost of the sale and foreclosing lien, the excess goes to pay off junior liens in order of priority.
4. The property owner (borrower) retains possession during foreclosure proceeding.
5. If the sale does not cover the loan amount, the lender may file for a deficiency judgment. But no deficiency judgment can be obtained for purchase money loans used to finance owner-occupied homes of four units or less.

### B. Trustee's sale (trust deeds)

1. No lawsuit necessary; foreclosure made by public sale
2. Requires three months' notification of default; also, within 10 days of recording notice of default, copy must be sent to trustor
3. Notice of sale
4. Property sold to high bidder at trustee's sale; title transferred under a trustee's deed
5. Deficiency judgments not allowed on nonjudicial foreclosures

### C. Deed in lieu of foreclosure

1. Alternative to foreclosure—mortgagor/trustor deeds to mortgagee/beneficiary
2. Disadvantage to lender—does not wipe out junior liens

## III. METHODS OF DEBT REPAYMENT/DEBT SERVICE

### A. Term (straight)

1. Interest only until maturity at end of term
2. Entire principal in one lump sum

### B. Fully amortized

1. Equal payments of principal and interest such that the balance becomes "zero"
2. Interest usually paid in arrears

**C. Partially amortized/balloon**

1. Equal payments of principal and interest
2. Balloon before end of term

**D. Graduated payment**

1. Lower payments in beginning, then they increase, then they level off
2. May have negative amortization (principal may increase)

**E. Adjustable-rate mortgage (ARM)/trust deed**

1. Rate subject to change based on changes in an economic index
2. May include interest and/or payment caps

**F. Reverse annuity mortgage/trust deed**

1. Payments paid to mortgagor over specific term
2. Due upon sale of property, death of mortgagor(s), or at the end of the term

**IV. TYPES OF TRUST DEEDS (AND MORTGAGES)**

**A. Package**

1. Personal property included as security in addition to real property
2. May be used to finance the purchase of a furnished condominium, etc.

**B. Blanket**

1. More than one property is pledged as security.
2. A release clause allows a subdivider to remove individual parcels as they are sold.

**C. Seller carryback purchase money**

1. Owner financing where title transfers to buyer
2. Seller “takes back” a trust deed/mortgage as partial payment; seller has lien

**D. Conventional/insured conventional**

1. Debt repayment is based solely on the borrower’s ability to pay; loans are not insured or guaranteed by the government.
2. Depending on the loan-to-value ratio, the lender may require private mortgage insurance (PMI).
3. If required, the PMI premium is paid to Mortgage Guarantee Insurance Corporation (MGIC).

**E. Construction**

1. Interim financing made available in installments as improvements are completed
2. Typically adjustable rate/short term from commercial banks
3. Lender may require a commitment for “take out;” a takeout loan replaces the construction loan with longer-term financing

**V. MISCELLANEOUS MORTGAGE TERMS****A. Loan-to-value ratio/mortgage ratio**

1. Maximum percentage of value lender will loan
2. Based on price or appraisal, whichever is less

**B. Equity**

1. Market value today  
– total debt today  
equity today
2. Leverage is the use of debt financing of an investment to maximize the return per dollar of equity invested.

**C. Points/loan origination fee**

1. Discount points are charged by the lender to increase the lender's yield.
  - a. One point = 1% of loan amount
2. A loan origination fee is charged by the lender to process and issue a loan.
3. Points can be used to lower the interest rate.

**D. Other clauses**

1. A subordination clause allows a change in the order/priority of mortgages.
2. A prepayment penalty clause allows a borrower to pay off the loan early, but the lender can charge punitive interest, which is taxed as interest and not cost of sale.

**VI. SOURCES OF CAPITAL FOR REAL ESTATE LOANS****A. Commercial banks**

1. Prefer short-term loans for commercial, business, and new construction

**B. Savings and loan associations**

1. Conventional, Federal Housing Administration (FHA), and VA home loans

**C. Mortgage bankers and mortgage brokers**

1. Mortgage brokers act as intermediaries between borrowers and lenders, but they don't usually service loans.
2. Mortgage bankers originate and service loans with deposits and personal money.

**D. Life insurance companies/credit unions/pension funds**

1. Prefer long-term commercial and industrial participation loans
2. Lender receives interest plus an equity position in income-producing properties

**VII. GOVERNMENT PROGRAMS**

Funds come from qualified lenders approved by the Department of Housing and Urban Development (HUD).

**A. FHA fully insured financing**

1. FHA insures lender against loss due to foreclosure
2. Enables high loan-to-value ratio
3. Mutual mortgage insurance (MMI) premiums may be paid at closing or financed
4. Property must meet minimum property requirements (MPRs)

**B. VA fully guaranteed financing**

1. Guarantees lenders against loss on loans to veterans
2. Can have up to 100% loan-to-value ratio
3. Two certificates required: certificate of eligibility and certificate of reasonable value (CRV)

**C. Miscellaneous aspects of FHA/VA**

1. Rules regarding assumption depend on the date of the loan
2. No prepayment penalty
3. Nonveterans may assume VA loans

**D. California Veterans Farm and Home Purchase Act (CalVet)**

1. The California Department of Veterans Affairs administers the program and is a direct lenders.
2. CalVet purchases the property, then resells it to the veteran under a real property sales contract/land contract; the veteran has equitable title and gets legal title when the loan is repaid.
3. The veteran is required to acquire a life insurance policy that will pay off the loan in case of death.
4. Impound accounts (reserves) are also required and there cannot be a prepayment penalty.

**E. The Federal Reserve Bank (The Fed)**

1. The nation's central bank, charged with regulating the nation's money supply
2. Regulates rate of growth/inflation

**F. Secondary mortgage market**

1. Where loans are bought and sold; NOT originated
2. Organizations that sell mortgage-backed securities to investors
3. To verify the loan balance upon purchasing the mortgage, the investor or secondary market purchaser will ask for a beneficiary statement
4. Discounting—when a loan is sold for less than its face amount

**VIII. FINANCING/CREDIT LAWS****A. Regulation Z/Truth in Lending—Federal Reserve Board regulates**

1. **Purpose:** promote the informed use of consumer credit by requiring meaningful disclosures about its terms and cost
2. Applies only to loans from institutional lenders to consumers for personal, family, or household purposes

**B. Real Estate Settlement Procedures Act (RESPA)**

1. Standardizes closing practices for certain transactions
2. Restricts amount of advance escrow payments for taxes and insurance
3. Lender must give prospective borrowers a *Your Home Loan Toolkit* booklet and a Loan Estimate form indicating the terms of the loan and of all closing costs within three business days from receiving the loan application
4. The lender is required to give borrower the Closing Disclosure form at least three business days before closing on the mortgage loan
5. Prohibits “kickbacks” for unearned fees, such as lenders, insurance agencies, escrow companies, or home protection companies paying money for referrals by brokers

**IX. LOAN BROKERAGE****A. Mortgage loan disclosure statement**

1. Disclosure required for all loans negotiated by licensees for one- to four-family residential transactions
2. Must be signed by both borrower and licensee and delivered to borrower before the borrower becomes obligated
3. Broker lending personal funds must disclose this fact

**B. Types of loan originators**

1. The SAFE Act is a federal law that provides for the licensing and registration of mortgage loan originators (MLO).
2. Three types of MLOs can operate in California:
  - a. Mortgage loan brokers (MLBs)
  - b. California finance lenders (CFLs)
  - c. Residential mortgage lenders (RMLs)
3. MLOs must complete 20 hours of education and pass a national and state exam.
4. MLOs must complete 8 hours of continuing education annually.

# UNIT 3 REVIEW QUESTIONS

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## True/False Questions

1. California is a title theory state.
  - A. True
  - B. False
2. With a deed of trust, title is given by the trustor to the trustee.
  - A. True
  - B. False
3. The financing document that serves as evidence of the debt is the deed of trust.
  - A. True
  - B. False
4. A promissory note is a negotiable instrument.
  - A. True
  - B. False
5. Term loans offer interest-only payments until maturity.
  - A. True
  - B. False
6. A package mortgage includes real property as well as personal property as collateral.
  - A. True
  - B. False
7. One parcel is used as collateral in a blanket mortgage.
  - A. True
  - B. False
8. Commercial banks prefer long-term financing.
  - A. True
  - B. False
9. Mortgage bankers act as intermediaries.
  - A. True
  - B. False
10. Mortgage brokers lend their own money.
  - A. True
  - B. False
11. Life insurance companies prefer long-term commercial and industrial participation loans.
  - A. True
  - B. False
12. FHA loans provide insurance to lenders against loss due to foreclosure.
  - A. True
  - B. False
13. Department of Veterans Affairs (VA)-guaranteed loans are available to those men and women who served in the U.S. armed forces and to their spouses.
  - A. True
  - B. False
14. Mortgage brokers offer CalVet loans.
  - A. True
  - B. False
15. The evidence of the debt for a mortgage or a deed of trust is a promissory note.
  - A. True
  - B. False
16. Covenants included in a security instrument are causes of foreclosure.
  - A. True
  - B. False
17. A deed of trust is a two-party instrument.
  - A. True
  - B. False
18. When a mortgage note is paid, the mortgagee records a deed of reconveyance.
  - A. True
  - B. False
19. Regulation Z/Truth in Lending promotes the informed use of consumer credit by requiring meaningful disclosures about the cost and terms of credit.
  - A. True
  - B. False
20. Annual percentage rate includes third-party costs.
  - A. True
  - B. False

21. The Real Estate Settlement Procedures Act prohibits kickbacks.
  - A. True
  - B. False
22. Discount points are charged by the lender to increase the lender's yield.
  - A. True
  - B. False
23. Advertising by a mortgage loan broker must include a statement that the broker is licensed by the California Department of Real Estate.
  - A. True
  - B. False
24. A broker is not allowed to lend his own funds.
  - A. True
  - B. False
25. The maximum commission that a broker can charge for negotiating or making a loan depends only on the amount of the loan.
  - A. True
  - B. False
26. A California finance lender is allowed to make loans with personal property as collateral.
  - A. True
  - B. False
27. The SAFE Act is a federal law that provides for the licensing and registration of mortgage loan originators (MLOs).
  - A. True
  - B. False
28. MLOs must complete 20 hours of continuing education annually.
  - A. True
  - B. False

### Multiple-Choice Questions

1. An individual selling a piece of property wanted to be sure that she would be relieved of primary liability for the existing loan on the property. Assuming that the existing loan was transferred to the buyer, which of the following would be MOST correct?
  - A. The buyer must take the property "subject to" the existing loan.
  - B. The buyer must pay cash.
  - C. The buyer is to assume the existing loan.
  - D. The buyer is to insure the seller against liability.
2. Which is a correct statement?
  - A. The effective interest rate is the interest rate paid, and the nominal interest rate is the minimal rate that is charged.
  - B. The nominal interest rate is the percentage of interest that is actually paid by the borrower, and the effective interest rate is the percentage of interest that is stated in the loan.
  - C. The effective interest rate is the percentage of interest that is actually paid by the borrower, and the nominal interest rate is the percentage of interest that is stated in the loan.
  - D. The nominal interest rate is the same as the annual percentage rate (APR).
3. Liquidation of a financial obligation on an installment basis is
  - A. acceleration.
  - B. amortization.
  - C. conventional.
  - D. conversion.
4. A person who is an innocent purchaser of a negotiable note for value without knowledge of any defect is customarily called
  - A. an assignor.
  - B. a receiver in trust.
  - C. an endorser in blank.
  - D. a holder in due course.
5. The MOST important factor to a lender who is contemplating a loan to a developer of a shopping center would be
  - A. the long-term leases.
  - B. the credit of the purchaser.
  - C. the number of tenants.
  - D. the anchor tenant.

6. An investor purchased an apartment building with a very small down payment and was able to secure financing for the balance. A year later, he sold the property for profit with no increase in his investment. This is an example of
  - A. debt reduction.
  - B. leverage.
  - C. appreciation.
  - D. inflation.
7. The quickness with which assets can be converted into cash is known as
  - A. yield.
  - B. leverage.
  - C. liquidity.
  - D. risk.
8. Which would NOT likely cause a loss to a lender?
  - A. Inflation
  - B. Recession
  - C. Unemployment
  - D. Prepayment without a penalty
9. The secondary money market creates a marketplace for the transfer of mortgages between which parties?
  - A. Mortgagors and mortgagors
  - B. Mortgagees and mortgagors
  - C. Mortgagees and mortgagees
  - D. Trustors and mortgagees
10. Which factor would be LEAST likely to influence the level and movement of mortgage rates?
  - A. Inflation
  - B. Tight money
  - C. Unemployment
  - D. Demand for funds
11. In real estate finance, a beneficiary statement refers to
  - A. the amount of profit realized by a lender.
  - B. the terms of a lease.
  - C. the amount of principal due on a loan.
  - D. the amount of money an heir would inherit.
12. What is the lender's BEST protection against default if the purchaser makes no down payment?
  - A. Low interest rate
  - B. Length of loan
  - C. Low monthly payments
  - D. Appreciation of the property
13. In a real estate transaction, a prepayment penalty is usually paid by
  - A. the buyer.
  - B. the lender.
  - C. the seller.
  - D. none of these.
14. The factor that exerts the greatest influence on mortgage interest rates is
  - A. the condition of the money market.
  - B. the value of the property.
  - C. the term of the loan.
  - D. the offsetting influence of conservative vs. nonconservative lenders.
15. Which is NOT a result of a subordination clause?
  - A. Permits a first trust deed to be refinanced and extended without losing priority
  - B. Allows for a construction loan to take priority
  - C. Causes hardship on the buyer by placing the lender of a larger sum in the favored position
  - D. Is more of a risk to the seller and may cause increased cost of the land and a more stringent release clause
16. The term *default* in MOST mortgages commonly means that the mortgagor
  - A. is delinquent in monthly payments.
  - B. is not using the property for its intended purpose.
  - C. failed to maintain the property.
  - D. did any of these.
17. Interest rates will normally decline when
  - A. inflationary trends accelerate.
  - B. the Federal Reserve Board increases reserve requirements.
  - C. there is an excess of mortgage funds available.
  - D. the federal budget deficit is high.
18. The person who would benefit the MOST from appreciation of a mortgaged property would be
  - A. the trustor.
  - B. the trustee.
  - C. the beneficiary.
  - D. none of these.

19. In setting up a release schedule under a blanket encumbrance, the beneficiary will usually require a disproportionate amount of money to release a particular lot

- to have better security on the remaining lots.
- because the best lots usually sell first.
- to protect the investment as individual lots are sold.
- for all of these reasons.

20. Regarding warehousing operations with respect to real estate finance, what would apply?

- Contract for sale
- Long-term debentures insured collaterally by real estate loans
- The mortgage banker collecting loans before sale
- Holding notes for investment

21. There was a second trust deed for \$5,000. The holder sold it to a friend for \$3,500. In the language of real estate practice, this would be known as

- liquidating.
- discounting.
- hypothecation.
- depreciation.

22. The loan-to-value ratio in a mortgage is defined as

- the monthly payment of the loan on a mortgage.
- the amount of a loan as a percentage of the appraised value.
- the amount of a loan as a percentage of the purchase price.
- the amount of a loan as a percentage of the assessed value.

23. Depending on the availability of funds and market rates, the rate of interest MOST likely to be charged is

- a variable interest rate.
- an interior loan rate.
- a fluctuating money market rate.
- the rate charged on a short-term land contract of sale.

24. When referring to real estate finance, the term *impounds* MOST nearly means

- moratorium.
- attachment.
- reserves.
- penalty.

25. A low loan-to-value ratio indicates

- a large loan.
- a low down payment.
- a high equity.
- a government-guaranteed loan.

26. Lenders have become confident and have been lending up to 95% on residential mortgages due to the availability of

- Fannie Mae insurance.
- mortgage cancellation insurance.
- guaranteed mortgage insurance.
- private mortgage guaranty insurance.

27. An agreement with a lender that prohibits early payoff of a loan is known as

- a prepayment penalty.
- an exculpatory clause.
- an open-end mortgage.
- a lock-in clause.

28. Most lending institutions are limited as to the amount they can lend, the types of loans they offer, and the length of loans. Because of certain limitations, some lenders are not interested or are unable to give construction loans, but are willing to issue long-term financing after the construction is completed. Long-term loans, to be issued by one lender upon completion of the interim construction financing by another lender, are known as

- discount loans.
- takeout loans.
- redemption loans.
- renewal loans.

29. Which definition BEST describes an open-end mortgage?

- One in which personal property is held for added collateral
- One in which the mortgage represents a partial payment for the parcel of the land
- One in which additional financing could be obtained without rewriting the contract
- One under which several parcels of land are included under one mortgage

30. A balloon payment would be a characteristic of

- a partially amortized loan.
- an amortized loan.
- a self-liquidating loan.
- a standing loan.

31. A person who wanted to transfer equitable title and retain legal title would use

- a mortgage.
- a grant deed.
- a security agreement.
- a land contract.

32. A broker negotiates a hard money loan secured by a deed of trust for which he receives a commission. In this transaction, hard money MOST nearly means

- a tight money loan.
- a secondary loan.
- a cash loan.
- a purchase money loan.

33. A real property sales contract is defined as an agreement wherein one party agrees to convey title to another party upon the satisfaction of specified conditions set forth in the contract and that

- must be acknowledged by both buyer and seller to be eligible for recording.
- does not require conveyance of title within one year from date of formation of the contract.
- must be recorded to be enforceable.
- is not required to be in writing if the contract period is for one year or less.

34. A “tight money” situation in which the Federal Reserve Board has taken action to reduce the money supply would MOST likely result in an increase in

- new first trust deeds and mortgages.
- new second trust deeds and mortgages.
- new home construction.
- real estate sales.

35. What is the MOST important influence affecting the interest rates on trust deed loans?

- Exchange rate overseas
- Gross national product
- Supply and demand of funds
- None of these

36. All of the following are advantages of FHA financing EXCEPT

- low mortgage insurance costs protect the borrower.
- short-term financing is eliminated.
- building standards are improved.
- the loan amount is appropriate for the borrower's income.

37. FHA mortgage insurance program loans for homes, as part of HUD, are made by

- FHA.
- VA.
- FNMA.
- banks, savings and loans, or mortgage companies.

38. A subdivider desiring to know the maximum FHA financing for a property would MOST likely go to

- an FHA appraiser for a firm FHA commitment.
- an FHA appraiser for a conditional commitment.
- a conventional lender for a firm FHA commitment.
- a lender for a conditional commitment.

39. FHA charges a premium to insure a mortgage. Premiums are designed to compensate the lenders if and when a borrower defaults on the FHA-insured mortgage. Which statement is TRUE with regards to most FHA loans?

- Premiums are paid up front and annually.
- Premiums must be paid entirely in cash.
- Premiums are only paid annually in the loan.
- The seller must pay the MIP.

40. In a period of inflation, the Federal Reserve Board would take which action to curb inflation?

- Reduce reserve requirements
- Lower discount rates
- Raise reserve requirements and sell bonds
- Raise discount rates and buy bonds

41. If the Federal Reserve Board wanted to create a tight money market, it would

- lower discount rates.
- raise discount rates.
- raise discount rates and buy bonds.
- lower discount rates and sell bonds.

42. When the Federal Reserve Board raises the discount rate to its borrowers, it has what effect on the money market?

- Has no effect
- Makes more marginal loans available
- Makes money more available
- Makes money less available

43. A bank will usually make a conventional loan and charge a higher interest rate than the interest rate charged on an FHA loan on the same property. What would be the determining factor in choosing to make an FHA loan instead of a conventional loan?

- Higher return
- Degree of risk
- Needs of the borrower for lower interest
- Number of properties sold by the seller

44. A buyer seeking an FHA loan would be LEAST likely to

- find a lender willing to give him the loan.
- go to the nearest FHA office for an appraisal.
- agree to pay mutual mortgage insurance.
- agree to make amortized payments.

45. Points are NOT charged on which type of home loans?

- Federal Housing Administration
- Veterans Administration
- California Department of Veterans Affairs
- None of these

46. Under which loan would the borrower be required to apply for term life insurance?

- FHA
- VA
- Savings and loan company
- CalVet

47. What is included in an FHA loan?

- Prepayment penalty
- Secondary financing
- Schedule of payments
- Mortgage life insurance

48. In the lending field, if there is a conflict in the note and mortgage provisions,

- the note provisions will generally control.
- the note is the security instrument.
- a mortgage gives validity to an unenforceable note.
- the mortgage provisions will generally control.

49. A three-party instrument in which real property is used as security for a loan is

- a chattel agreement.
- a bill of sale.
- a trust deed.
- a certificate of sale.

50. Johnson agreed to purchase Smith's property and to use the existing conventional loan of record on the property. Johnson agrees to relieve Smith of primary liability. The loan balance is \$80,000 payable at \$784 per month, including 11% per annum. In accordance with Johnson's agreement, which of the following is the correct insertion on the deposit receipt?

- Buyer to take property subject to loan of record
- Buyer to make payments according to first trust deed term
- Buyer to agree to insure seller against all liability on existing trust deed
- Buyer to assume existing first trust deed

51. Which would hold equitable title?

- Trustor under a deed of trust
- Vendee under a land sales contract
- Both trustor under a deed of trust and vendee under a land sales contract
- Neither trustor under a deed of trust nor vendee under a land sales contract

52. A due-on-sale clause, whether it is enforceable or not, contained in a mortgage or trust deed is a type of

- acceleration clause.
- defeasible clause.
- executed clause.
- legally enforceable clause.

53. A statement provided by the payor on a promissory note that would list payments, term period of the note, principal balance, interest, et cetera is called

- beneficiary statement.
- release clause.
- request for partial reconveyance.
- offset statement.

54. A clause in a second trust deed that permits the first trust deed to be refinanced without affecting its priority would be known as

- an alienation clause.
- an acceleration clause.
- a subordination clause.
- a lien waiver.

55. Who benefits MOST from a subordination clause in a trust deed?

- Trustor
- Trustee
- Beneficiary
- None of these

56. Broker Wilson sells a house, and a loan for the buyer is secured through a savings and loan association. Wilson carefully explains all loan costs to the buyer. According to the Real Estate Settlement Procedures Act (RESPA), which statement is TRUE?

- The lender must provide an estimate of settlement costs to the buyer immediately.
- The lender must provide the buyer with a Loan Estimate within three business days.
- Broker Wilson must provide the buyer with an estimate of settlement costs within one week.
- Broker Wilson would not have to provide an estimate of settlement costs to the buyer because he had explained all costs.

57. The three-day right of rescission provided under the federal Truth in Lending Act would *MOST* likely apply to

- a first trust deed loan to purchase a home using FHA, VA, or conventional financing.
- a first trust deed loan to purchase a new business or commercial property.
- a first trust deed loan to purchase a house for rental.
- a new second trust deed loan against a home.

58. The Jacksons bought a residence with a first trust deed loan from a savings and loan. The Londons bought a residence with a first trust deed loan from a bank. The Londons refinanced, obtaining a first trust deed loan from a savings and loan, to get money for a business opportunity. Which statement is correct?

- The Jacksons do not have the right of rescission, the Londons do.
- The Londons do not have the right of rescission, the Jacksons do.
- Both have the right of rescission.
- Neither has the right of rescission.

59. Under the provisions of the Real Estate Settlement Procedures Act, which would NOT be considered a violation?

- Kickbacks
- Unearned fees
- Buyer designating lender
- Seller designating title insurance company

60. Under the Real Estate Settlement Procedures Act (RESPA), lenders are required to give borrowers

- a bill of sale.
- a Loan Estimate.
- the amount of mortgage interest.
- an invoice not exceeding \$10 for the special information booklet.

61. What is included as part of the finance charge in a Truth-in-Lending Disclosure Statement?

- Appraisal fee
- Assumption fee
- Recording and document fees
- Title insurance fees

62. According to the Federal Reserve System's Regulation Z, which would be the proper usage in an advertisement relating to housing?

- Assume a 7½% mortgage
- Assume a 7½% annual percentage rate mortgage
- Take over a 7½% mortgage
- Any of these

63. Which loan costs are NOT required to be disclosed as a finance charge to the customer under federal truth-in-lending rules?

- Credit investigation
- Buyer's points
- Time-price differential
- Finder's fees

64. Which would be covered by the Real Estate Settlement Procedures Act (RESPA)?

- Land for development
- An addition of a room in a single-family residence
- A commercial building
- An initial lien on a one-to-four-unit residential building

65. Under the Truth in Lending Act, a Notice of Cancellation could be given when the loan was

- used for business expansion.
- more than \$25,000 and was not secured.
- secured by the owner's residence.
- secured by a commercial building.

66. Don Sanderson, a real estate broker, works alone in his independent brokerage firm, Sanderson Real Estate. Sanderson helps clients buy and sell commercial real estate, and manages property for owners of income-producing property. Sanderson also serves as a broker for mortgage loans, bringing together prospective borrowers with prospective lenders. Which of the following statements is correct?

- Sanderson's real estate license authorizes him to work as a mortgage loan broker.
- Provided Sanderson has an MLO endorsement on his real estate license, serving as a mortgage loan broker is legal.
- Serving as a mortgage loan broker is always illegal for real estate licensees.
- Real estate licensees serving as mortgage loan brokers may not legally receive compensation for their mortgage loan brokerage activities.

67. Regarding the fees and commissions a mortgage loan broker can charge for regulated loans, all of the following statements are correct EXCEPT

- for regulated loans, the commissions that loan brokers can charge are limited, but the costs are not.
- California law regulates the fees and commissions a loan brokerage firm can charge for regulated loans.
- the ceiling placed on loan broker commissions is an exception to the general rule that commissions are negotiable.
- regulated loans are first mortgages of less than \$30,000 and second mortgages of less than \$20,000.

68. Which lender participates in and supervises construction loans, solicits loans from anyone, involves itself in the secondary money market, and represents other lending institutions?

- Insurance company
- Mortgage company
- Commercial bank
- Savings and loan association

69. A certain lender has the following lending policies and characteristics:

Makes many loans on commercial properties  
Makes relatively few construction loans  
Usually seeks to avoid administering loans  
Prefers to make long-term loans  
This describes which lender?

- Life insurance companies
- Federal savings and loans
- Mortgage companies
- Savings and loan associations

70. A primary source of funds for residential financing is

- the Federal Home Loan Bank.
- the Federal Savings and Loan Insurance Corporation.
- the Federal Savings and Loan Association.
- the Federal Housing Administration.

71. The lenders that invest a major portion of their assets in long-term real estate loans do not like to service their own loans and that like large loans on commercial property would be

- commercial banks.
- insurance companies.
- savings and loan associations.
- mutual mortgage companies.

# UNIT 4

## Laws of Agency and Fiduciary Duties

### LEARNING OBJECTIVE

*When you have completed this unit, you will be able to accomplish the following.*

- ♣ Describe real estate laws of agency and fiduciary duties in California.

#### I. PARTIES TO AN AGENCY RELATIONSHIP

##### A. Principal

1. One who employs another to act on his behalf
2. Consumer principal is a “client”

##### B. Agent/fiduciary

1. One who is employed to represent a principal
2. Fiduciary is the highest trust relationship under law—must put the client’s interest above one’s own

##### C. Third party

1. A party to a transaction who is not a party to the particular agency agreement
2. Consumer third-party buyer is a “customer”
3. Agent of principal owes duties of fair dealing and disclosure of material facts to third party, but not fiduciary duties

## II. TYPES OF AGENCY AND CREATION OF AGENCY

### A. Types of agency

1. Special agency = listing agent authorized by a listing agreement
2. General agency = property manager
3. Attorney in fact is authorized to perform in place of the principal; accomplished through power of attorney

### B. Creation of agency

1. Express agency is created through an oral or written agreement (before the fact).
2. Agency by ratification is created after the fact, when a previously unauthorized action is confirmed by a principal.
3. Ostensible agency or agency by estoppel is created when a third party is led to believe an agency relationship exists.
4. Compensation is not a requirement of an agency relationship. Who pays the agent does not determine whom the agent represents.

## III. RESPONSIBILITIES OF AGENT/DISCLOSURE OF AGENCY

### A. An agent owes a principal/client fiduciary obligations (OLD CAR)

1. Obedience
2. Loyalty
3. Disclosure
4. Confidentiality
5. Accounting
6. Reasonable care and skill

### B. Disclosure of representation

1. Representation must be disclosed as soon as practical.
2. An agency disclosure form must be provided and signed before the signing of a listing or writing of an offer.
3. Confirmation of agency relationships is required before entering into a contract (process: disclosure, election, confirmation).
4. Disclosure if representing or working with a relative or any person with whom agent has significant relationship (e.g., best friend) is required.

5. If representation changes, a new disclosure is required at once.
6. When representing both the buyer and the seller (dual agency), the agent must get consent of both parties in writing—undisclosed dual agency.
7. Brokers owe those they don't represent honesty and fair dealing, even if the principal asks to lie or keep silent.

#### **C. Transfer disclosure statement (TDS)**

1. Required of both seller and agent with exceptions, which include foreclosures, co-owner to co-owner sales, or other examples where seller would not have knowledge of the property or would not need disclosure
2. Easton v. Strassburger decision requires licensees to disclose what they know and what they should know

#### **D. Additional disclosures/obligations**

(**Note:** See Practice and Mandated Disclosure Section for further discussion of disclosures)

1. Full fiduciary obligation of disclosure to client
2. Disclosure of material facts to customer
3. Must present all offers; multiple offers should be presented at the same time
4. Listing agreements generally authorize broker to collect earnest money deposits along with offers; if not authorized to do so, broker can accept deposits, but becomes an agent of the buyer for that deposit
5. Earnest money/deposits
6. Must disclose that commissions are negotiable in listing agreement

#### **E. Liability for another's acts**

1. Each broker is responsible for the professional actions of the salespeople the broker employs.
2. A principal is responsible for misrepresentations made by an agent within the scope of the agent's authority.

#### **F. Multiple listing service (MLS)**

1. The MLS is a widely used arrangement in which brokers pool listings and offer cooperation to other brokers.
2. Cooperating brokers must obey all the laws of agency.

**IV. THE LISTING AGREEMENT**

A listing agreement is a personal service contract/employment contract between a broker and a seller that establishes an agency relationship and grants the broker the authority to seek buyers and obtain offers.

**A. Types of listings**

1. Exclusive right to sell
2. Exclusive agency
3. Open/nonexclusive
4. Net listing
5. Option listing

**B. Essential elements of a listing**

1. In writing and signed by the owner to be enforceable
2. Amount/method of compensation paid to the listing broker is negotiable
3. Price and terms
4. Definite beginning and termination date for exclusive listings
5. Agent's authority

**C. How a listing terminates**

1. Performance by both parties (completion of the sale)
2. Expiration of term
3. Revocation by principal/renunciation by broker/mutual rescission
4. Death or incapacity of either broker or seller (Note: death of salesperson does not terminate a listing). Listings belong to the broker.
5. Destruction of premises
6. Bankruptcy of either broker or seller

**D. When commissions are earned**

1. When broker procures a ready, willing, and able buyer
2. When seller accepts an offer presented by a broker

**V. BUYER AGENCY AGREEMENT****A. Types of buyer representation agreements**

1. An exclusive right to represent authorizes one broker to represent the buyer and requires the buyer to compensate the agent when purchasing property through any source.

**VI. BROKER/SALESPERSON RELATIONSHIPS****A. Employment contract**

1. Regulations of the real estate commissioner require brokers to have a written agreement with a salesperson.
2. Under real estate law, salespeople are employees of the broker, even if the contract defines them as independent contractors for tax purposes.

**B. Internal Revenue Service (IRS)**

1. The IRS may classify a salesperson as an employee or an independent contractor.
2. Employees are under the direct control of their employers and can be told how to perform the job.
3. Independent contractors are compensated based on results; employers have less control over how the job is done.

# UNIT 4 REVIEW QUESTIONS

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## True/False Questions

1. An agent is a person who is employed to represent or act for someone else in dealings with third parties.
  - A. True
  - B. False
2. The brokerage firm owns all contracts.
  - A. True
  - B. False
3. All real estate licensees are independent contractors.
  - A. True
  - B. False
4. Independent contractor licensees must have a signed employment agreement with their broker.
  - A. True
  - B. False
5. The law of agency specifies fiduciary duties to the principal, best remember by the acronym OLD CAR.
  - A. True
  - B. False
6. A dual agent represents only one party to a transaction.
  - A. True
  - B. False
7. A special agent is created when an agent is authorized to perform a series of acts associated with the continued operation of a particular business.
  - A. True
  - B. False
8. An agency relationship can be created by express or implied agreement only.
  - A. True
  - B. False
9. An express agency must be in writing.
  - A. True
  - B. False
10. An implied agency is created through an agent's actions.
  - A. True
  - B. False
11. Agency by ratification is created after the fact, when a previously unauthorized action is confirmed by a principal.
  - A. True
  - B. False
12. Agency by estoppel is also called ostensible agency.
  - A. True
  - B. False
13. A principal may evade the agency relationship in an agency by estoppel.
  - A. True
  - B. False
14. The laws of agency specify fiduciary duties owed to the principal.
  - A. True
  - B. False
15. An agent must obey the lawful instructions of the principal.
  - A. True
  - B. False
16. An agent must place the interest of the principal above all others.
  - A. True
  - B. False
17. The agent must make full disclosure of all material facts concerning the transaction to the principal.
  - A. True
  - B. False
18. An agent must keep the principal's confidential information private.
  - A. True
  - B. False

19. It is acceptable for agents to gain a secret profit as a result of the relationship with a principal.  
A. True  
B. False

20. As a licensed professional, you will be held to a higher standard.  
A. True  
B. False

21. Representation can be disclosed within three business days of signing the listing agreement.  
A. True  
B. False

22. A written document that explains the various relationships of those involved in a residential property sale must be presented to both buyer and seller as soon as practicable.  
A. True  
B. False

23. Disclosure, election, and confirmation is the three-step process of confirmation of agency relationships required before entering into a contract.  
A. True  
B. False

24. The fact that an agent is representing a relative in a transaction does not have to be disclosed.  
A. True  
B. False

25. The Civil Code requires specific wording to be included in the agency disclosure form.  
A. True  
B. False

26. If representation changes, a new disclosure is required at once.  
A. True  
B. False

27. A general agent has the authority to perform a single act for the principal.  
A. True  
B. False

28. A special agent has the ability to bind their principal.  
A. True  
B. False

29. A power of attorney is a written agreement whereby a principal appoints an agent, known as an attorney-in-fact, to act in their place.  
A. True  
B. False

30. Dual agency occurs when a broker represents more than one party to a transaction.  
A. True  
B. False

31. Undisclosed dual agency is legal.  
A. True  
B. False

32. Agents who represent themselves without the knowledge of the third party would be subject to disciplinary action.  
A. True  
B. False

33. Agents owe no duties to those they don't represent.  
A. True  
B. False

34. The principal or agent may not terminate the agency unilaterally.  
A. True  
B. False

35. The person who terminates the agency may be liable for damages to the other party.  
A. True  
B. False

36. Notice of termination must be given to third parties with whom the principal and the agent are dealing.  
A. True  
B. False

37. The ways in which an agency relationship may be terminated are specified by the Department of Real Estate.  
A. True  
B. False

38. Death of the sales associate would terminate an agency.  
A. True  
B. False

39. Expiration of the term or fulfillment of the agency agreement are two ways to terminate an agency.

- True
- False

40. Agents are not responsible for disclosing to the principal any conflict of interest.

- True
- False

41. If the aunt of a broker wants to make an offer on a house listed by the broker, the relationship does not have to be disclosed to the seller.

- True
- False

42. An agent's commission is earned when the escrow closes.

- True
- False

43. The principal can revoke the agency agreement without any liability.

- True
- False

44. In an open listing, if the seller accepts an offer that was not secured by the listing broker, the seller need not compensate the listing broker.

- True
- False

45. Exclusive right-to-sell listings offer the protection to listing brokers that they will receive a commission regardless of who procures the buyer.

- True
- False

46. In exclusive agency listings, the listing agent will receive a commission even if the seller finds the buyer.

- True
- False

47. An agent must disclose material facts to a third party.

- True
- False

48. Material facts must not be disclosed if the principal asks the agent to keep silent.

- True
- False

49. Disclosure of material facts is not required for properties being sold "as is."

- True
- False

50. A material fact can be anything that would affect the value or desirability of the subject property.

- True
- False

51. *Easton v. Strassburger* is the landmark real estate case on disclosure to third persons.

- True
- False

52. Agents owe fair dealing to those they don't represent.

- True
- False

### Multiple-Choice Questions

1. Attorneys-in-fact with general powers can do all of the following EXCEPT
  - sign the name of their principal.
  - perform certain acts under a general power of attorney.
  - deal in real estate without recording their power of attorney.
  - encumber their principal's property with a trust deed wherein another person is the beneficiary.
2. A real estate broker may NOT accept a listing from a minor appointing the broker as her agent because
  - a minor does not have capacity to enter into contracts.
  - a minor is legally incapable of appointing an agent.
  - the broker would breach his fiduciary relationship by misrepresenting a minor who is incapable of making adult decisions.
  - the minor has the right to disaffirm the listing contract during her minority.

3. A licensed real estate salesperson takes a listing that does not authorize her to take a deposit. The salesperson finds a buyer, however, who gives her a personal check as a deposit with an offer on the property. With regard to the deposit, the salesperson's broker would be
  - A. the agent of the seller.
  - B. the agent of the buyer.
  - C. the agent of the bank.
  - D. required to place the check in escrow.
4. A person delegated in an instrument to act legally for another in his stead is
  - A. power of attorney.
  - B. attorney-in-fact.
  - C. principal.
  - D. trustee.
5. In a sales transaction, the broker acted as an agent for both the buyer and the seller and collected a commission from each. He failed to disclose to either that he was receiving a commission from the other party. In this case, after the close of escrow, which of the following could happen?
  - A. The broker could be disciplined by the Department of Real Estate.
  - B. The broker could be denied any commission.
  - C. The buyer could rescind the purchase.
  - D. Any of these could happen.
6. A real estate broker could be held liable to a buyer if she
  - A. unknowingly makes a misrepresentation to the buyer based on false information given by the seller.
  - B. executes an agreement with the buyer on behalf of the seller under a power of attorney granted by seller.
  - C. retains the buyer's check at the seller's request after an offer has been accepted by the seller and acceptance has been communicated to the buyer.
  - D. acts in excess of the authority given by the seller under a listing agreement.
7. Martin contacted his broker, Katz, to list a property for sale for \$200,000. Martin indicated to the broker that he needed a quick sale of the property. The broker contacted a prospective buyer and told him that Martin would sell the property for \$180,000. The buyer made an offer in the amount of \$180,000, which Martin accepted when the broker presented it to him. Under these conditions, Katz
  - A. violated the fiduciary relationship but did no harm because the offer was accepted.
  - B. violated the fiduciary relationship because he acted in excess of authority given to him.
  - C. did not violate the fiduciary relationship because Katz was employed by Martin and acted under such authority.
  - D. did not violate the fiduciary relationship because the offer was accepted.
8. What BEST describes an attorney-in-fact?
  - A. A person with a dual agency
  - B. A lawyer acting as an attorney for a client
  - C. A lawyer appointed by the court
  - D. A legally competent person appointed to represent another person through a power of attorney
9. All of these people can sue a third party for specific performance EXCEPT
  - A. an attorney-in-fact acting for the principal.
  - B. the seller of a large tract of land.
  - C. the purchaser of a residential property.
  - D. a broker acting as the agent for the principal.
10. All of these are necessary for the creation of an agency agreement EXCEPT
  - A. mutual agreement of the parties.
  - B. competency of the seller.
  - C. consideration.
  - D. fiduciary relationship.

11. A seller owns a large parcel of land in a rural area. The seller owns surface, subsurface, and air rights to the property. From speaking to a government official, the listing agent discovers that valuable minerals lie beneath the surface of the land. A prospective buyer is not represented by any real estate licensee. To whom should the listing agent disclose the valuable subsurface mineral rights under the surface of the subject property?

- A. The seller only (Positive material facts need only be disclosed to the property owner.)
- B. The seller and the prospective buyer
- C. The seller only (The listing agent only owes a fiduciary duty of disclosure to the seller.)
- D. The buyer only (The listing agent can assume the seller is already aware of the subsurface minerals.)

12. A broker was working conscientiously and diligently for a buyer under a written exclusive right-to-buy buyer representation agreement. The buyer, Samantha Chan, found a property and made a written offer without the assistance of her broker. The seller accepted the offer and communicated acceptance directly to the buyer. The seller was selling the property without the assistance of an agent. Does Samantha Chan have to pay a commission to her broker?

- A. No. Because the buyer found the property herself, the buyer's broker has not earned a commission.
- B. No. The buyer's agent didn't exercise due diligence to find a property the buyer liked.
- C. Yes. Because the seller was working without a broker, the buyer's broker is said to be working "in house."
- D. Yes. The buyer's broker earns a commission, if a property is found within the term of the buyer representation agreement.

13. Broker A had a listing and cooperated with Broker B on an offer from a buyer procured by Broker B. The seller accepted the buyer's offer and the transaction was placed in escrow. It is due to close within two or three days when Broker A learns that Broker B has arranged a sale of similar acreage at a considerably higher price to the same buyer. In these circumstances, what should Broker A do?

- A. Notify the seller of the higher price
- B. Do nothing because of the imminent closing
- C. Attempt to renegotiate a higher price
- D. File an interpleader action and obtain a writ of replevin

14. Antonia Bui, a seller, hired a listing agent to sell her three-unit residential property. Bui had inherited the property from her father and had substantial experience with both buying and selling realty. Before the listing agreement was signed, the agent presented an agency disclosure form to the seller. The listing agent marketed the property and solicited several offers. Bui accepted an offer, and the transaction closed. All of the following statements are incorrect EXCEPT

- A. the agency disclosure form is only required for single-family residences.
- B. agents must only present the agency disclosure form to buyers.
- C. the agency disclosure form is a legal requirement only for first-time buyers or sellers.
- D. the agency disclosure form should be presented to the seller before the listing agreement is signed by the seller.

15. ABC Brokerage firm has 175 salespeople and 50 broker associates. Many of the associates work remotely. Barbara Smith, a broker associate, took a listing for 100 Oak Tree Lane #A, a condominium. Jessica Kahn, a salesperson, worked for a buyer looking for a condominium unit. Neither Smith nor Kahn knew each other. The buyer made an offer on the condo, the seller communicated acceptance, and escrow subsequently closed. After the close of escrow, the seller discovered that Barbara Smith and Jessica Kahn both worked for ABC Brokerage firm. Which of the following statement(s) is correct?

- A. If the broker of record is the same for Barbara Smith and Jessica Kahn, this was an undisclosed dual agency.
- B. The DRE disciplines real estate licensees for undisclosed dual agencies.
- C. An undisclosed dual agency may result in the disgorgement of any earned commission
- D. All of these.

16. Which of the following parties may NOT serve only as the selling agent?

- A. The buyer's agent
- B. Both parties
- C. Neither party
- D. The listing agent

17. A property, a two-unit duplex, was jointly owned by Joan Fortin and her nephew, Ronald Brown. Brown was also serving as the listing broker for the property. In addition to his portion of the sales price and the commission earned as the listing agent, Brown also quietly collected \$1,000 at the close of escrow and did not inform his aunt. The failure to disclose the \$1,000 MOST likely made the listing broker

- liable to Joan Fortin for the \$1,000.
- subject to discipline by the DRE.
- the recipient of a secret personal profit.
- all of these.

18. Rosa Lopez asked her listing broker to recommend an escrow company. The listing broker recommended ABC Escrow. The listing broker did not disclose that his spouse worked at—and had an ownership interest in—ABC Escrow. The failure to disclose the employment and ownership interest by the listing broker's spouse in the recommended entity was

- legal because the listing broker did not work at, or own, ABC Escrow.
- legal, provided that the listing broker did not profit from the recommendation.
- illegal because the listing broker should have disclosed the spouse's interest in the recommended entity.
- illegal because it is never acceptable for an agent to recommend an entity owned by family members.

19. The seller and the listing agent entered into an exclusive listing agreement for a commercial office building located in an area at risk for wildfires. During the term of the listing contract, the office building burned down. What impact, if any, will the destruction of the improvements have on the listing agreement?

- There will be no impact because real estate is considered indestructible.
- The destruction of the improvements will terminate the listing agreement.
- The listing agreement for the commercial office building will, through operation of law, be transformed into a listing agreement for vacant land.
- If the listing agent had notice that the property was located in an area subject to wildfires, the listing agent must continue to exercise due diligence to find a buyer.

20. Robert Wilson, a real estate salesperson with 20 years' experience, worked for Best Realty Brokerage. Wilson canvassed a neighborhood and found an owner who agreed to list the property with Best Realty Brokerage and then signed an exclusive listing agreement. Wilson put a tremendous amount of time and effort into marketing the property, and four offers on the property were submitted at an open house on Saturday. Late Sunday night, Wilson had a heart attack and died. What impact will Wilson's death have on the listing agreement?

- The death of the salesperson will have no effect on the listing agreement.
- The death of the salesperson will automatically terminate the listing agreement.
- The death of the salesperson will shorten the term of the listing agreement.
- The death of the salesperson will extend the term of the listing agreement.

21. A seller and a listing agent entered into an exclusive listing agreement for the sale of a large parcel of real estate improved with a single-family residence. The listing agent received several offers, the seller accepted an offer, and escrow closed three months later. At the time of the closing, the listing agent received the agreed-upon commission from the seller. Which of the following statements is correct?

- This listing agreement is an executory contract, and there is still an agency relationship between the seller and the listing agent.
- A listing agreement terminates 6 months after the close of escrow.
- This listing agreement is an executed contract, and the agency relationship between the seller and the listing agent was terminated at the close of escrow.
- A listing agreement terminates 12 months after the close of escrow.

22. An agent may collect a commission for a negotiated sale after the term of the listing contract expired if

- the agent signs a release clause.
- the agent sues the principal for liquidated damages.
- the contract contains a protection period clause.
- there is an alienation clause.

23. The maximum amount of commission and loan costs that may be charged for a second trust deed of \$4,000 for a four-year term is

- \$550.
- \$725.
- \$850.
- \$990.

24. On an exclusive right-to-sell agreement, an owner may

- revoke the agreement but not be liable for damages.
- revoke as long as he sold the property himself.
- revoke the agreement but may be liable for damages.
- not revoke because this is a binding contract.

25. A real estate licensee negotiated the sale of a farm for a seller. The agent's commission can be paid in which form?

- Assignment of funds from buyer to seller
- Assignment of existing note
- Check or cash
- Any of these

26. A listing agent gave part of his commission to the buyer. He

- is guilty of criminal action.
- is guilty of committing a civilly wrong act.
- may be disciplined by the real estate commissioner.
- must disclose this to the seller.

27. A listing broker told a prospective buyer that the subject property had the best view of the city in the entire subdivision. The buyer, unrepresented by any real estate agent, went to other open houses at that same subdivision. The buyer saw several other properties with, what the buyer thought, were better views of the city. The listing broker MOST likely engaged in which of the following activities?

- Misrepresentation
- Puffing
- Perjury
- Breach of the listing broker's fiduciary duty to the buyer

28. At an open house, a prospective buyer asked a listing agent whether the hardwood floors were real wood. Which of the following would have been an appropriate reply?

- "I don't know. Let me find out and get back to you."
- "No. It's laminate wood flooring."
- "According to the seller, the floor is true mahogany wood."
- All of these.

29. A prospective buyer belongs to a racial minority. The listing broker was asked by the prospective buyer about racism in the neighborhood. The listing broker knew that several acts of a racist nature had recently occurred nearby and had been reported to the police. None of those racist acts had been committed against—or on—the subject property. Does the broker need to disclose this knowledge to the prospective buyer?

- No. None of the alleged acts happened on the subject property.
- Yes. The reported acts are material facts that need to be disclosed.
- Yes. These racist acts indicate the perpetrators are involved in panic peddling.
- Yes, but only if the racist acts were perpetrated against the minority group to which the prospective buyer belonged.

# UNIT 5

## Practice of Real Estate and Disclosures (Includes Specialty Areas)

### LEARNING OBJECTIVE

*When you have completed this unit, you will be able to accomplish the following.*

- ♣ Describe the practice of real estate and disclosures (includes specialty areas) in California.

#### I. FAIR HOUSING

##### A. Civil Rights Act of 1866

1. The Civil Rights Act of 1866 prohibits discrimination based on an individual's race.

##### B. Civil Rights Act of 1968—Title XIII Fair Housing Act

1. Race (only protected class in the 1866 Civil Rights Act)
2. Religion
3. Color
4. National origin
5. Sex (added in 1974)
6. Family status (added in 1988)
7. Handicap/disability (added in 1988)

**C. California fair housing laws**

1. Include the Unruh Civil Rights Act, the Fair Employment and Housing Act (Rumford Act), the Housing Financial Discrimination Act (Holden Act), and the California Fair Employment and Housing Act (FEHA)
2. Stricter than federal acts; add protected classifications of physical disability; mental disability or medical condition; marital status; sex or sexual orientation; age, with respect to persons over the age of 40; and pregnancy, childbirth, or related medical conditions

**D. Prohibited actions**

1. Less favorable treatment (including refusal to show property)—the only time it would be okay to not show a home to a member of a protected class would be if the owner had given an instruction to not show the home to anybody for a legal reason (e.g., illness)
2. Discriminatory or restrictive advertising
3. Steering the channeling of potential buyers to or away from particular areas as a means of discrimination
4. Blockbusting—also called panic peddling; inducing people to sell their homes because of the entry into the neighborhood of members of protected classes
5. Redlining—refusing to offer or limiting loans in certain areas

**E. Americans with Disabilities Act (ADA)**

1. Ensures equal access to public accommodations for disabled persons
2. Requires removal of architectural and communication barriers when “readily achievable”
3. Also prohibits employment discrimination against disabled persons if a company has 15 or more employees

**F. Servicing diverse populations**

1. The goal of servicing diverse populations is inclusion.
2. Parties that constitute diverse populations include the following:
  - a. Victims of domestic violence
  - b. Individuals in transition (e.g., returning veterans)
3. Real estate professionals should be prepared to serve clients from various backgrounds.

**G. California Civil Code**

1. This allows disabled tenants to make changes at their expense. The owner may require the tenant to return property to the original condition upon termination of lease.

## II. TRUST ACCOUNTS AND RECORDKEEPING

### A. Trust accounts

1. The purpose of trust fund accounting is to keep a broker's funds separate from the broker's clients.
2. Commingling of trust funds with funds belonging to the licensee is prohibited and is a misdemeanor; the actual use of trust funds for purposes other than their intended purpose is conversion and is a felony.

### B. Recordkeeping

1. Brokers are responsible for maintaining adequate and accurate records.
2. Brokers must reconcile the trust accounts on a monthly basis to check that the money in the account is equal to their liability.
3. Most accounts must be kept for three years and must be open for inspection by the real estate commissioner.
4. Brokers may use electronic image storage media to retain and store copies of all listings, deposit receipts, canceled checks, trust records, and other documents—so long as they provide, at their own expense, a paper copy of any document or record requested by the DRE.

### C. Advance fees

1. An advance fee is the collection of an up-front fee for performing services involving real property for buyers, sellers, lenders, or borrowers. Used properly, they are legal.
2. A person who proposes to collect an advance fee must submit all materials and agreements to the commissioner no less than 10 calendar days before publication or use.
3. The law prohibits a licensee from claiming, collecting, or receiving an advance fee involving a loan modification or forbearance before performing the services contracted for or represented that the licensee would perform.

## III. DEPARTMENT OF REAL ESTATE (DRE) DISCIPLINARY ACTIONS

### A. Composition and powers of the DRE

1. The Department of Real Estate operates within the California Department of Consumer Affairs and is led by the real estate commissioner.
2. The real estate commissioner is appointed by the governor.
3. Powers of the DRE include regulation of licensees and subdivisions.
4. The DRE does NOT mediate commission disputes or collect penalties for victims of licensees.

### B. Violations of the real estate law—examples of unlawful conduct

1. Knowingly misrepresenting value of property to get a listing or secure a buyer

2. Representing to an owner when seeking a listing that the licensee has obtained a written offer when the licensee has no such offer
3. Stating or implying that the licensee is prohibited by law or regulation from charging less than the quoted commission
4. Misrepresenting the licensee's relationship with a broker or the broker's responsibility for acts of the licensee
5. Knowingly underestimating closing costs
6. Knowingly making a false or misleading representation regarding the form, amount, and/or treatment of an earnest money deposit
7. Knowingly making a false or misleading representation to a seller financing part of a sale regarding buyer's ability to pay
8. Making an addition or modification to the terms of an agreement previously signed by a party without the knowledge and consent of the party
9. When acting as a principal for real estate paper, making a representation regarding the value of securing property without reasonable basis for believing it is accurate
10. Making a representation regarding the nature and/or condition of the features of a property, the size or boundaries of the property, or the legal use of the property without having a reasonable basis for believing it to be true
11. When acting as an agent, failing to disclose to a prospective purchaser material facts about the property
12. When acting as a listing agent, failing to present any written offer unless instructed by the owner not to present such an offer
13. When acting as a listing agent, presenting competing offers in a manner that would induce the owner to accept an offer that provides greater compensation to the agent
14. Failing to explain to the prospective parties for whom the licensee is acting as an agent the meaning and probable significance of a contingency in an offer or contract that may affect the closing date
15. Failing to disclose to a seller whom the licensee represents the nature and extent of any direct or indirect interest that the licensee expects to acquire as a result of the sale.
  - a. Also must disclose if a relative or person with whom licensee has a special relationship may be acquiring an interest; same rule applies to representing a buyer and having an interest in the property buyer may acquire
16. Failing to disclose to a principal any significant interest the licensee has in an entity the agent recommends
17. When acting as an agent for the seller, refunding any part of an offeror's deposit after the seller has accepted the offer, unless the licensee has express permission from the seller to make the refund

**C. Unlicensed assistants**

1. The DRE provides brokers with the following guidelines for activities which unlicensed assistants may perform:
  - a. Assist licensees at an open house by placing signs, greeting the public, handing out preprinted materials, or providing factual information prepared by and approved by the licensee
  - b. Cold call or canvass to develop general information about the interest of the person or to make an appointment, but not for solicitation purposes
  - c. Prepare a comparative market analysis subject to the approval of and for use by the licensee
  - d. Arrange for inspections and order reports and services from third parties (e.g., a pest control inspection or roof inspection, or repair work), or be present to let such individuals into the property
  - e. Prepare and design advertising that is reviewed and approved by the broker
2. Only a licensee can perform the following activities:
  - a. Only a licensee may show or exhibit the property, discuss terms and conditions of a possible sale, or discuss other features of the property, such as its location, neighborhood, or schools.
  - b. Information needed by third parties, for the purpose of completing her report, must typically be provided by the licensee.
  - c. At no time may an unlicensed assistant attempt to induce a person to use a licensee's services.

**D. Commission rebates to buyers and sellers**

1. It is unlawful for any real estate licensee to pay any compensation for performing acts for which a license is required to an unlicensed individual; however, payments made by a licensee to a principal in a transaction does not constitute a violation of the law according to the DRE.
2. If there is a commission rebate to a buyer in a transaction that fact must be disclosed by the agent to the seller who has paid the commission.

**IV. CONSUMER RECOVERY ACCOUNT****A. Purpose**

1. Portions of license fees are placed into an account from which members of the public can be compensated for illegal acts of licensees.
2. Funds can be disbursed if a judgment has been obtained and the debt is uncollectible from the licensee.
3. The license is suspended until the licensee makes payment back to the fund.

**B. Limits**

1. \$50,000 limit per transaction
2. \$250,000 limit against one licensee

**V. TRUTH IN ADVERTISING****A. False advertising is grounds for revocation or suspension of a license****B. Blind advertising**

1. Blind Advertising does not list the name of an agent where an agent is involved.
2. All advertising of an activity for which a license is required must indicate a licensee designation ("agent" would meet the requirement).

**VI. MANDATED DISCLOSURES****A. Natural hazards disclosure form**

1. Sellers and agents must sign the following:
  - a. Earthquake disclosures
  - b. Dam failure inundation
  - c. Very-high fire hazard zone
  - d. Wildfire risk areas
  - e. 100-year flood zones

**B. Environmental hazards pamphlet**

1. In addition to disclosing environmental (as opposed to natural) hazards in the TDS, sellers and agents can provide a prepared pamphlet.
2. If the pamphlet is provided, neither the seller nor the agent has a duty to provide further information regarding environmental hazards (except for lead-based paint disclosure) unless there is actual knowledge.

**C. Mello-Roos disclosure**

1. The seller of a one- to four-unit dwelling must disclose if the property is subject to a Mello-Roos lien.

**D. Seller financing disclosure**

1. If there is seller financing, the Seller Financing Addendum and Disclosure form is required.

**E. Other required disclosures**

1. Megan's law—all purchase contracts must include a notice informing buyers or lessees of the public availability of information regarding registered sex offenders
2. Home energy ratings
3. Home inspection notice—for FHA financing or HUD-owned property, borrower must sign notice (“Importance of a Home Inspection”)
4. Smoke detector notice
5. Water heater bracing
6. Carbon monoxide alarms

**VII. PROPERTY MANAGEMENT/LANDLORD-TENANT****A. License requirement**

1. A real estate license is required for property managers who rent, lease, solicit listings of places for rent, solicit for prospective tenants, and collect rents.
2. A license is not required for a resident manager, if management activities are confined to the complex in which the manager lives.

**B. Security deposits**

1. The amount of security deposits that can be collected:
  - a. Maximum security deposit, unfurnished unit—2 times rent
  - b. Maximum security deposit, furnished unit—3 times rent
2. Under California law, within 21 days of tenants moving out, the landlord must either
  - a. send tenants a full refund of their security deposit, or
  - b. mail or personally deliver to tenants an itemized statement that lists the amount of any deductions from the security deposit and the reason for the deductions, with a refund of any amount not deducted.

**C. Landlord warrants**

1. Warranty of quiet enjoyment—lease will not be disturbed by someone claiming paramount title
2. Warrant of habitability—landlord must keep property in livable condition
3. If these are violated, tenant may have right of constructive eviction

**D. Unlawful detainer**

1. A court action by a lessor to regain possession (eviction) upon default (e.g., nonpayment of rent)
2. Notice to quit required

**VIII. MOBILEHOMES AND MANUFACTURED HOMES****A. License requirements**

1. Real estate licensees can sell used mobilehomes that have been registered with the Department of Housing and Community Development (HCD) or are in place on a lot.
2. Licensees cannot sell new mobilehomes or maintain a place of business where two or more mobilehomes are displayed unless they are also licensed as a mobilehome dealer.

**B. Advertising and Disclosures**

1. Licensees must withdraw advertisements within 48 hours of receipt of notice it is no longer available for sale or lease
2. Cannot represent a used mobilehome as being new
3. Cannot represent a mobilehome is capable of being transported on a highway when it doesn't meet equipment requirements

# UNIT 5 REVIEW QUESTIONS

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## True/False Questions

1. Trust funds refer to money or anything of value received by an agent, but not belonging to the agent.
  - A. True
  - B. False
2. Commingling is the stealing of trust funds.
  - A. True
  - B. False
3. Trust fund records must be kept for three years.
  - A. True
  - B. False
4. All brokers must maintain a trust account.
  - A. True
  - B. False
5. The Civil Rights Act of 1866 prohibits discrimination in every property transaction.
  - A. True
  - B. False
6. In 1968, Congress enacted the federal Fair Housing Act based on the goal of fair housing throughout the United States.
  - A. True
  - B. False
7. Steering is the prohibited action of discriminatory advertising.
  - A. True
  - B. False
8. Redlining is the refusal to loan in designated areas.
  - A. True
  - B. False
9. Blind advertising is committed when a licensed real estate agent fails to disclose the fact that they are licensed.
  - A. True
  - B. False
10. All advertising of an activity for which a license is required must indicate the name and designation of the licensee.
  - A. True
  - B. False
11. Any advertising for a mobile home for sale must be withdrawn within 48 hours after receipt of notice that it is no longer available for sale.
  - A. True
  - B. False
12. Only a mobile home that meets vehicle code requirements can be represented as transportable on a California highway.
  - A. True
  - B. False
13. Sales associates are responsible for maintaining adequate and accurate records.
  - A. True
  - B. False
14. Brokers must reconcile trust accounts on a monthly basis.
  - A. True
  - B. False
15. Trust funds may be deposited in a certificate of deposit account.
  - A. True
  - B. False
16. A broker may keep up to \$200 of her own funds in a trust account.
  - A. True
  - B. False
17. The sales associate owns all contracts.
  - A. True
  - B. False
18. Employing brokers are responsible for supervision of employees but not of independent contractors.
  - A. True
  - B. False

19. It is a regulation of the real estate commissioner that brokers have a written employment contract with all salespersons they supervise.
  - A. True
  - B. False
20. The employing broker must withhold income taxes from independent contractors.
  - A. True
  - B. False
21. Unlicensed sales assistants are allowed to make telephone calls to canvass for interest in using the services of a real estate broker.
  - A. True
  - B. False
22. Unlicensed sales assistants may NOT be present in an open house.
  - A. True
  - B. False
23. Unlicensed sales assistants may prepare a comparative market analysis (CMA).
  - A. True
  - B. False
24. Unlicensed sales assistants may give access to a property.
  - A. True
  - B. False
25. The regulations of the real estate commissioner have the force and effect of law.
  - A. True
  - B. False
26. The real estate commissioner has the power to administer and enforce the Subdivided Lands Law.
  - A. True
  - B. False
27. Only a district attorney can suspend a real estate license.
  - A. True
  - B. False
28. If a formal hearing is held as a result of a complaint, the commissioner becomes the respondent and the licensee is the complainant.
  - A. True
  - B. False
29. An application for a real estate license must be honest and truthful.
  - A. True
  - B. False
30. The salesperson's exam contains 150 questions, of which at LEAST 80% must be answered correctly to pass.
  - A. True
  - B. False
31. The full term for a broker's or salesperson's license is two years.
  - A. True
  - B. False
32. To renew a license for an additional four years, the licensee must successfully complete 45 hours of continuing education.
  - A. True
  - B. False
33. The Recovery Account is financed by property taxes.
  - A. True
  - B. False
34. The Recovery Account is available to aid victims of licensee fraud, misrepresentation, deceit, or conversion of trust funds.
  - A. True
  - B. False
35. The maximum amount collectible per transaction is \$75,000.
  - A. True
  - B. False
36. Upon payment from the Recovery Account, the offender's license is revoked.
  - A. True
  - B. False
37. Ethics is usually expressed as a set of principles or values.
  - A. True
  - B. False
38. The REALTOR® Code of Ethics is based on the Golden Rule.
  - A. True
  - B. False

39. All immoral acts are illegal.  
A. True  
B. False

40. To promote ethical business practices, the real estate commissioner has suggested that licensees strive to provide equal opportunity to all persons.  
A. True  
B. False

41. Real estate professionals require high-powered computers.  
A. True  
B. False

42. Access to a multiple listing service is one of the major reasons why real estate professionals need to have a computer.  
A. True  
B. False

43. A National Association of REALTORS® training program to certify real estate professionals as internet professionals is the e-PRO certification.  
A. True  
B. False

44. The cloud refers to storing data on a provider's server, as opposed to on an individual's computer.  
A. True  
B. False

45. No license is required to be a property manager.  
A. True  
B. False

46. Certified Property Manager (CPM) is a designation for members of the Institute of Real Estate Managers.  
A. True  
B. False

47. In California, every building of 12 or more dwelling units must have a resident manager.  
A. True  
B. False

48. The property manager ordinarily earns a base salary.  
A. True  
B. False

49. Commercial real estate agents may specialize in a type of property.  
A. True  
B. False

50. Industrial property agents make relatively few sales per year.  
A. True  
B. False

51. Real estate licensees seldom sell residential income property.  
A. True  
B. False

52. Because of fixed rents, landlords under rent control often reduce maintenance and defer repairs.  
A. True  
B. False

53. Real estate licensees can only sell business opportunities if they include the real property.  
A. True  
B. False

54. Vacant lot sales cannot be handled by real estate licensees.  
A. True  
B. False

55. The sale of time-shares is another area of specialization.  
A. True  
B. False

56. Real estate licensees who are licensed as mortgage loan originators may act as lenders in making and arranging loans.  
A. True  
B. False

57. The Transfer Disclosure Statement (TDS) details the mechanical and structural conditions of the property.  
A. True  
B. False

58. The Transfer Disclosure Statement is to be completed by the listing agent.  
A. True  
B. False

59. An exemption from the Transfer Disclosure Statement would be a foreclosure sale.  
A. True  
B. False

60. Other items included in the Transfer Disclosure Statement are the age of the roof, any unpermitted additions, encroachments, and easements.  
A. True  
B. False

61. The Natural Hazard Disclosure Statement must only be provided in single-family residential transactions.  
A. True  
B. False

62. The law requires sellers to disclose to buyers if the property being sold lies within one or more mapped hazard areas.  
A. True  
B. False

63. Earthquake disclosures and dam failure inundation are two of the mapped hazard area requirements.  
A. True  
B. False

64. Only the seller signs the Natural Hazard Disclosure Statement.  
A. True  
B. False

65. All deaths that occurred in the property are considered material fact.  
A. True  
B. False

66. *Easton v. Strassburger* expanded the broker's duty of disclosure to third parties.  
A. True  
B. False

67. Agents have a duty only to their principals to disclose material facts.  
A. True  
B. False

68. If the escrow holder receives information regarding material facts concerning the transaction, such information should be disclosed immediately to the relevant parties.  
A. True  
B. False

69. The real estate agent's visual inspection is expected to replace the role of a professional home inspector.  
A. True  
B. False

70. All properties require the same types of inspections.  
A. True  
B. False

71. The agent's visual inspection will reveal any areas requiring further investigation.  
A. True  
B. False

72. The seller is responsible for payment of the structural pest control report.  
A. True  
B. False

73. The escrow officer is the one who receives all reports authorized by the escrow instructions.  
A. True  
B. False

74. Examples of such reports include a termite company report, a roof inspection report, as well as an electrical, a foundation, or a soil report.  
A. True  
B. False

75. Attending diverse cultural and community events can expand a licensees' client base.  
A. True  
B. False

76. Multicultural etiquette can lead to success with new clients and customers.  
A. True  
B. False

77. The goal of servicing diverse populations is exclusion.  
A. True  
B. False

### Multiple-Choice Questions

1. A licensee who is guilty of conversion is one who is
  - misrepresenting.
  - misappropriating the funds of clients.
  - commingling.
  - failing to make full disclosure.

2. Johnson, who owns a ranch, gave Otis, a broker, an exclusive listing to sell the property. Johnson also advanced Otis \$100 to advertise the sale of this ranch in a brochure published by Otis. The real estate law requires that brokers account for such funds by placing the \$100
  - A. in the broker's trust account in order that the money may be returned to the seller if the property is not sold.
  - B. in the broker's trust account, expend from the trust account only for advertising the property, and provide a report to the seller that will itemize all expenditures made.
  - C. in the broker's personal office account and spent only for advertising the property.
  - D. in the broker's trust account in case the seller defaults.
3. The balancing of a broker's trust account record to the bank balance is known as
  - A. posting.
  - B. trial balance.
  - C. closing out the books.
  - D. reconciliation.
4. The purpose of a trust account is to
  - A. provide for the commingling of the trust funds and the brokers funds.
  - B. provide easy disbursement of funds.
  - C. keep the broker's funds and trust funds separated.
  - D. do none of these.
5. A buyer made an earnest money offer to purchase property, and the broker placed the funds in his trust account. After the seller's acceptance but before opening of escrow, the buyer informs the broker that he has revoked his offer and demands the return of the deposit. The broker, not wanting to be involved in the conflict with respect to the disposition of the deposit funds, deposited them with the appropriate court. This would be an example of
  - A. assignment.
  - B. equitable disposition.
  - C. interpleader.
  - D. surrender.
6. Robert Smith signed an offer and gave the broker his personal check made payable to an escrow company as a deposit. He stipulated that the broker was to hold the check until his offer was accepted by the seller. The listing agreement specified that any deposit money must be a cashier's check made payable to the seller. Under these circumstances, the broker should
  - A. submit the offer and deposit the check in escrow.
  - B. submit the offer and hold the check.
  - C. hold the check but do not reveal to the seller that he has accepted the check until the seller accepts the offer.
  - D. refuse to accept a deposit that does not conform to the precise terms of the listing.
7. A large cosmetics plant is being built in a small town. A developer plans to build a new subdivision to provide housing for the new workers who will be moving into town. The developer recognized that most of the employees of the cosmetics plant will be women. In setting up a sales program, the developer gave instructions that (1) the advertising was to be pointed toward a preference for women buyers and (2) the properties should be sold equally to Caucasians, Blacks, Chicanos, and Asians. As the quota for each group was sold, other members of that group would be discouraged from buying through increasing prices to them and advising them that no properties were available. Which of these instructions would be in violation of the fair housing laws?
  - A. Item (1) only
  - B. Item (2) only
  - C. Both items (1) and (2)
  - D. Neither item (1) nor item (2)
8. A seller asked the listing broker the ethnic background of a prospective buyer. Should the listing broker disclose this information?
  - A. The broker must disclose this information.
  - B. Disclosure may be made but the broker must tell the seller it cannot affect the decision because of the California Fair Housing Law.
  - C. The broker should ask the buyer's broker if it is all right to advise the seller of the buyer's ethnic background.
  - D. No. Disclosure is against the Rumford Act.

9. A broker was intentionally renting only to members of the Caucasian race. Under the Unruh Civil Rights Act, the broker would be
  - A. liable to pay the aggrieved person \$250 in penalties.
  - B. held liable for actual damages incurred by the aggrieved party.
  - C. subject to suspension or revocation of his real estate license.
  - D. all of these.
10. The federal Fair Housing Act contains provisions to prevent discrimination due to race, color, religion, sex, or national origin. A violation of this law would be considered
  - A. against public policy.
  - B. unlawful.
  - C. illegal.
  - D. all of these.
11. A real estate licensee is canvassing an area in order to secure listings for an office. The agent tells the prospective sellers that minority groups are moving into the area and it would be advantageous to sell at this time. If the licensee canvasses in this manner, she
  - A. would be disciplined by the real estate commissioner for canvassing in this manner.
  - B. would not be disciplined by the real estate commissioner because this is a legitimate selling tactic.
  - C. would not be disciplined by the real estate commissioner if the broker had instructed her to canvass in this manner.
  - D. would not be disciplined by the real estate commissioner if the prospective sellers were members of a minority group.
12. A minority prospect came to you and asked to see a specific house in a minority neighborhood. You can lawfully assume that the prospect is
  - A. interested in a house in a minority neighborhood.
  - B. interested in a house with a particular type of architectural style.
  - C. trying to test you.
  - D. unable to qualify for VA or FHA housing and you should refuse to show the prospect any houses.
13. The federal Fair Housing Act was enacted for the purpose of
  - A. equal but separate housing within the states.
  - B. providing fair housing for minority groups.
  - C. providing fair housing opportunity for all persons throughout the United States.
  - D. elimination of prejudice throughout the United States.
14. A licensee put a blind ad in a local newspaper. A blind ad does NOT
  - A. identify the advertiser as an agent.
  - B. give the address of the licensee.
  - C. give the address of the property.
  - D. disclose the selling price.
15. A real estate salesperson who advertises a property must provide in the advertisement
  - A. the broker's name.
  - B. the broker's name and address.
  - C. both the salesperson's name and their 8-digit DRE license number.
  - D. both the broker's name and address and the salesperson's name.
16. A broker placed advertisements on her listings as follows. Which of these would come under the provisions of the Truth in Lending Act?
  - A. "2 bedrooms, large lot, nothing down"
  - B. "3 bedrooms, 1 bath, \$21,000, excellent GI-FHA financing"
  - C. "3 bedrooms, den, \$25,500, E-Z terms"
  - D. "4 bedrooms, family room, owner will help finance"
17. In accordance with the Truth in Lending Act, what must be included in the advertisement for a graduated payment mortgage loan?
  - A. The location of the property
  - B. The address of the lender
  - C. The name of the broker
  - D. The amounts of different monthly payments

18. Do all advertisements of real estate brokers that contain real estate credit terms come under the Truth in Lending Act?

- Yes, there are absolutely no exceptions to Regulation Z.
- No, there are exceptions to Regulation Z.
- It depends because Regulation Z does not pertain to amounts above \$25,000.
- Regulation Z does not apply because this matter does not come under the Truth in Lending Act; it comes under the jurisdiction of the proper licensing agency.

19. What is the minimum amount of time that a broker must keep signed copies of listings, deposit receipts, et cetera?

- One year
- Two years
- Three years
- Four years

20. In a transaction in which the sale of a property has resulted, the broker must keep a copy of the deposit receipt for three years from the date of

- deposit receipt.
- acceptance of offer.
- closing of transaction.
- recording of grant deed.

21. Ali Singh passed her broker's exam and immediately opened up her own independent real estate brokerage firm. Before passing her broker's exam, Singh had only two years of full-time experience in the real estate world. Prisha Patel has been a successful real estate broker for 15 years. Patel comes to work for Singh as a broker associate. Which of the following statements is correct regarding supervision?

- Because of her much greater professional experience, Patel will supervise Singh.
- Because both Singh and Patel are brokers, neither needs to be supervised.
- The daily real estate activities of both Singh and Patel will be supervised by the DRE.
- Patel must be supervised as if she were a real estate salesperson.

22. Real estate regulations require a broker to review and initial sales contracts and overview the activities of the employed salesperson. The law permits a broker to delegate this duty to

- a person licensed as a salesperson for two of the past five years.
- a person licensed as a salesperson for two of the past 10 years.
- a licensee who has been employed by the broker for two of the past five years.
- a licensee with two years' experience who has successfully completed 18 college credits in real estate.

23. Matthew Green, an unlicensed sales assistant, works for Christina Green, his wife and the broker of record for Christina Green's independent brokerage firm. Christina Green is the listing broker for a single-family residence located near the Green's family home. At an open house, Christina Green leaves to address a family emergency. Matthew Green is left alone at the open house for approximately 30 minutes. One prospective buyer arrived during this time, and, because the Greens lived nearby and had school-aged children, Matthew Green answered general questions about the athletic programs at the local public schools. Which of the following statements is correct?

- Because Matthew Green had actual knowledge of nearby athletic school programs, answering these general questions about local school programs was permissible.
- Only a licensee is allowed to discuss features of the property such as the neighborhood and nearby school programs.
- Provided Matthew Green did not discuss financing or offers, answering general questions about local school programs was permissible.
- Provided Matthew Green was approved to sit for the DRE state salesperson's exam, answering general questions about local school programs was permissible.

24. Alice Rossi has been working as an unlicensed real estate sales assistant for 25 years. She understands nearly all the documents needed to complete purchase transactions for commercial real estate. A buyer of a commercial office building calls the real estate brokerage firm to ask a question related to a provision in a purchase contract. The only real estate licensee available at the time has no experience with commercial real estate purchase contracts. Under these conditions, Rossi goes ahead and explained the provision in the document to the prospective buyer. Her explanation was informative and accurate. Which of the following statements is true?

- A. Because it was accurate, Rossi's explanation violated no laws.
- B. Because of her experience with that particular type of contract, Rossi's explanation violated no laws.
- C. Because the only available licensee lacked experience with this particular contract, Rossi's explanation violated no laws.
- D. None of these

25. An owner of a small investment company advertised and sold properties for a commission. In his advertisements, he did not indicate that he was a licensee, and in fact, he was not. He also made false statements in his advertising. Because he failed to disclose material facts, who would prosecute this person?

- A. Local law agencies
- B. District attorney
- C. Real estate commissioner
- D. Attorney general

26. Which of the following would be considered fraudulent misrepresentation?

- A. Agent makes a statement he knows is not true in order to induce a party to enter into a contract
- B. Agent makes a promise that he does not intend to fulfill
- C. Agent knowingly withholds a material fact
- D. All of these

27. Which of the following are considered to be violations of the Business & Professions Code, Real Estate Law, Commissioner's regulations, or the Subdivided Lands Law?

- A. Misuse of trade name
- B. Negligence or incompetence
- C. Failure to disclose ownership interest
- D. All of these

28. The real estate commissioner has the authority to

- A. create statutes to discipline licensees.
- B. issue licenses for out-of-state transactions.
- C. promulgate reasonable rules and regulations.
- D. settle disputes over commissions.

29. A salesperson unlawfully takes kickbacks in connection with licensed real estate activities. The employing broker finds out about the kickbacks, fires the salesperson, and warns others in the office not to do this. Under these circumstances,

- A. only the salesperson could be disciplined by the real estate commissioner.
- B. only the broker could be disciplined by the real estate commissioner.
- C. both the salesperson and the broker could be disciplined by the real estate commissioner.
- D. a court could revoke the salesperson's real estate license.

30. The required written agreement of broker-salesperson is a regulation of

- A. NAR.
- B. the Real Estate Board.
- C. the real estate commissioner.
- D. no one.

31. Which act or statement might be a cause for disciplining a licensee?

- A. A statement made to the seller that this is the highest offer the buyer will make
- B. A statement to the buyer that this is the lowest offer a seller will accept
- C. A statement to a buyer that "this is the best house on the street"
- D. Misrepresentation that did not result in a loss to the principal

32. A licensed real estate salesperson has been selling unimproved lots through the employing broker and receiving a finder's fee from a lender for referring the buyers to the lender. The broker discovers this and fires the salesperson and warns all the other salespeople not to be involved in this type of practice. If these facts come to the attention of the real estate commissioner,

- the commissioner has no cause for disciplinary action, even though it may be unethical.
- the broker but not the salesperson is subject to disciplinary action.
- the salesperson alone is subject to disciplinary action.
- both the broker and the salesperson may be disciplined.

33. According to Title VIII of the Civil Rights Act of 1968 and an 1866 law enacted by Congress, a person discriminated against in the purchase of a home because of race could go to court and the court could rule all of these EXCEPT

- revocation and suspension of broker or salesperson's license if the court concludes that the broker has discriminated.
- money damages for humiliation and embarrassment.
- money damages and punitive damage to prevent a recurrence.
- money damages and specific performance.

34. Which of the following licenses is not for a four-year term?

- A broker associate's license
- A broker's license
- A salesperson's license
- A PRLS license

35. A salesperson's license expired before completion of the required 45 hours of DRE-approved continuing education hours. After the salesperson's license expired, escrow closed on a property the salesperson had worked on diligently. Which of the following statements is TRUE?

- The salesperson will have four years to complete the required continuing education.
- The broker of record will not be able to split an earned commission with this salesperson.
- The salesperson will have to repeat the three licensing classes.
- The salesperson will have three years to complete the required continuing education.

36. What is the maximum amount that the Consumer Recovery Account will pay out to applicants?

- \$250,000 lifetime maximum per licensee
- \$50,000 per transaction
- Both of these
- Neither of these

37. During a single transaction related to the sale of real estate, a married couple suffered serious losses due to the intentional fraud perpetrated by a real estate licensee. The couple sued the licensee in court and won. The final judgment was for \$300,000. After the trial, the spouses diligently attempted to collect the judgment award from the licensee, but were unable to do so because the licensee had no money. The couple then applied to the DRE's Consumer Real Estate Recovery Fund, properly complying with all the DRE's application rules. Assuming the DRE determines that the applicants' claim is valid, how much will they be able to recover from the fund?

- The married couple will recover \$150,000 each, for a total of \$300,000.
- The married couple will recover a maximum of \$250,000.
- The married couple will recover a maximum of \$50,000 total.
- The married couple will recover \$50,000 each, for a total of \$100,000.

38. Who investigates and punishes ethical violations perpetrated by real estate licensees?

- A local district attorney
- The state DRE
- Both of these
- Neither of these

39. In 1913, the National Association of REALTORS® (NAR) adopted a Code of Ethics for real estate professionals. NAR regularly updates its Code of Ethics, as the professional responsibilities of real estate licensees change over time. To what extent are California real estate licensees legally bound by the NAR Code of Ethics?

- California real estate licensees are not legally bound by NAR's Code of Ethics.
- Violation of the NAR Code of Ethics will subject a licensee to discipline by the DRE.
- Violation of the NAR Code of Ethics will prevent a renewal of a real estate license.
- Violation of the NAR Code of Ethics will result a restricted real estate license.

40. A real estate salesperson wants to demonstrate up-to-date knowledge about real estate technology trends and advanced digital marketing techniques. To do so, the real estate salesperson received e-PRO® certification. Membership in which of the following organizations is required for e-PRO® certification?

- National Association of REALTORS® (NAR)
- California Department of Real Estate (DRE)
- National Association of Real Estate Appraisers (NAREA)
- U.S. Department of Housing and Urban Development (HUD)

41. When a tenant is delinquent in his rent under a written lease, the landlord may evict the tenant by

- giving a written three-day notice.
- filing a notice of default.
- bringing a court action.
- doing all of these.

42. A tenant who transfers an entire leasehold interest does so by

- sublease.
- transfer.
- assignment.
- alienation.

43. Which situation, where an extension of credit for more than four installments is made, would be exempt from the federal Truth in Lending Act?

- \$20,000 personal loan from a commercial institution
- \$20,000 household loan from a credit union
- Loan from a consumer finance company
- Purchase of agricultural land

44. A landlord and a tenant mutually agree to terminate a lease. This is often called

- rescission.
- surrender.
- release.
- abandonment.

45. Quiet enjoyment and possession usually refer to which circumstance?

- Neighbors creating a nuisance
- Noise abatement
- Possessory interest of a tenant given by the owner of the paramount title
- None of these

46. What would create an interest in property with possessory rights but no form of title?

- Mortgage
- Easement
- Sublease
- Land contract

47. A lessee may be justified in abandoning a rented dwelling if there is constructive eviction by the landlord. All of these would be constructive eviction EXCEPT

- condemnation of the entire property in eminent domain proceedings.
- failure of the landlord to repair excessive wear and tear to property caused by the tenant.
- an eviction notice is tendered by the landlord.
- unwarranted delays by the landlord after notice to make repairs of damages that have made the property unfit for occupancy.

48. Metal that is used in a roof to prevent water from seeping through is called

- mud sill.
- lath.
- soffit
- flashing.

49. To find the size of footings, the size and dimensions of concrete piers, construction measurements, and the details of the subfloor area, a real estate broker would look at

- the plot plan.
- the floor plan.
- the foundation plan.
- the elevation plan.

50. A contract between two or more persons where one grants the other the right to sell, offer to sell, or exchange goods or services under a marketing plan designed by the grantor is

- a franchise agreement.
- a business opportunity.
- a securities and exchange agreement.
- a financing agreement.

51. A licensee who has negotiated the sale of a mobile home would NOT be subject to discipline by the commissioner of real estate if she

- sent a check to the Department of Housing and Community Development drawn on an account that has insufficient funds.
- failed to deliver the certificate of registration to the Department of Motor Vehicles.
- sold a mobile home that is greater than 8 feet in width and 32 feet in length.
- advertised a mobile home as being new when it is not new.

52. In California, estates at will are created by

- a properly written and executed document.
- express agreement.
- operation of law.
- either express agreement or operation of law.

53. Under California law, it is necessary to give notice to terminate

- estate for years.
- estate at sufferance.
- estate at will.
- none of these.

54. Mr. and Mrs. Jenkins own a home worth \$533,000 on which there is a \$519,000 loan. Mrs. Jenkins alone filed a Declaration of Homestead. If a judgment lien were filed against them,

- the home would not be sold because there is insufficient equity over and above the exemption and the secured lien to satisfy the creditor.
- the home could be sold to satisfy the judgment.
- the homestead is invalid because only Mrs. Jenkins filed it.
- the exemption would be for \$10,000 because Mrs. Jenkins filed it without her husband's signature.

55. Considering the nature of real estate investments in that they are made over a long period of time, require a considerable amount of money, are harder to care for, and generally have a slower turnover, the return on these investments should be

- the same as first trust deeds.
- higher than bonds but lower than first trust deeds.
- the same as bonds.
- more than bonds and first trust deeds.

56. Mr. Borg purchased a new mobile home two months ago and contacted broker Wilson to take a listing on it. With respect to this information, Wilson

- could take a listing anytime but could not sell the mobile home for one year.
- could not list the mobile home unless she was also licensed by the Department of Motor Vehicles as a Vehicle Dealer.
- could not list the mobile home if it had not been registered with the Department of Housing and Community Development.
- could not take a listing and sell the mobile home unless it was installed on a foundation and properly registered with the county recorder.

57. Which of the following parties is not responsible for completing a portion of the Transfer Disclosure Statement (TDS)?

- Seller
- Buyer
- Listing agent
- Selling agent

58. A five-unit residential apartment building was built in 1975. The seller was aware that portions of the improvements were painted with lead-based paint. The seller was careful to disclose this to the listing broker at the time the seller signed the listing agreement. After the close of escrow, the buyer decided to manage the newly purchased apartment building without the assistance of a real estate licensee. There were already tenants living in two of the units, and the buyer quickly found and signed three new tenants to fill the apartment building. Legally, who had to receive a Transfer Disclosure Statement?

- The buyer
- The three new tenants
- Both of these
- Neither of these

59. Which of the following lists contains only those hazards on the Natural Hazards Disclosure Statement?

- Special Flood Hazard Area, Dam Failure Inundation, Asbestos, Wildland Fire Hazard, Earthquake Fault Zone, and Seismic Hazard Zone
- Special Flood Hazard Area, Dam Failure Inundation, Very High Fire Hazard, Wildland Fire Hazard, Mold, and Seismic Hazard Zone
- Special Flood Hazard Area, Dam Failure Inundation, Very High Fire Hazard, Wildland Fire Hazard, Earthquake Fault Zone, and Seismic Hazard Zone
- Special Flood Hazard Area, Radon Gas, Very High Fire Hazard, Wildland Fire Hazard, Earthquake Fault Zone, and Seismic Hazard Zone

60. Is the Natural Hazards Disclosure Statement a legally required part of the purchase contract for a single-family residence?

- Yes
- No
- No, unless the buyer is getting FHA fully insured financing
- No, unless the buyer is getting VA fully guaranteed financing

61. The broker took a listing from a seller and sold to a buyer for the full listed price and terms. After the sale, the seller discovered that the buyer is the brother of the broker. Under these circumstances,

- the broker was within the law.
- there would be a good cause of action against the broker only if the sale had been for less than the full listed price.
- there would be good reason to bring suit against the broker.
- none of these is true.

62. Examples of unlawful conduct under the Business and Professions Code include knowingly making a substantial misrepresentation of the likely value of real property to

- the owner to secure a listing.
- a prospect to induce them to make an offer.
- both the owner and the prospect.
- neither the owner nor the prospect.

63. A seller sued a real estate broker for misrepresentation of a material fact that the broker had made to him during the sale transaction. In defending the suit, the broker was able to prove that the listing contract with the seller had been an oral agreement. Under these circumstances,

- this is a valid defense based on the statute of frauds.
- the statute of frauds is not a bar in any real estate transaction litigation.
- this defense is not a bar because it was not the issue.
- the broker is only liable for misrepresentation to buyers.

64. An inspector was hired to complete a report on a recently listed single-family residence. The property was located at 100 Maple Leaf Lane. The inspector called the brokerage firm to get information about the listed property, and an unlicensed assistant answered the call. The unlicensed assistant looked up the requested information in a file for a recently closed property located across the street from 100 Maple Leaf Lane. The information on the recently closed property had been reviewed and approved by the broker of record before the closing. Was the action of the unlicensed assistant proper?

- Yes, because the information came from a recently closed transaction.
- No, an unlicensed assistant is never allowed to give information about a property to an inspector.
- No, an unlicensed assistant is only allowed to give information about a specific property when that information has been reviewed and approved by a licensee.
- Yes, because the information on the recently closed property had been reviewed and approved by the broker of record.

65. A developer of a new subdivision of five or more parcels must have a Subdivision Final Public Report (Public Report) before legally being able to close escrow on any of the newly divided parcels. Who provides the information used to create the Public Report and who issues it?

- A. The DRE provides the information, and the developer issues the Public Report.
- B. The developer provides the information, and the DRE issues the Public Report.
- C. The developer provides the information, and municipalities issue the Public Report.
- D. Municipalities provide the information, and the developer issues the Public Report

66. When is the BEST time for a seller to obtain a termite report?

- A. Before putting the house on the market
- B. Before determining the sales price
- C. Before opening escrow
- D. After the lender's appraisal

67. An escrow company received two termite reports in which the estimates of cost of the work differed. Under these circumstances,

- A. the seller and the broker must decide which report to use.
- B. the seller and the broker should present both reports to the buyer.
- C. the least expensive report should be used.
- D. the most expensive report should be used.

68. Three undergraduate students share an apartment near a local university. They each belong to a different race. The three roommates enjoy this diversity and want to expand upon it by bringing in a fourth roommate from a different race. They reach out to a real estate licensee for help in adding to the racial diversity in the apartment with an additional roommate. All of the following statements are incorrect EXCEPT

- A. because the goal is to enhance diversity, the real estate licensee can assist.
- B. because the goal is to include a different race, the real estate licensee can assist.
- C. because this would violate federal and state fair housing laws, the real estate licensee cannot assist.
- D. because there are shared living areas in the apartment, the real estate licensee can assist.

69. A married couple lived in a unit in a residential apartment complex. During an argument, the husband physically assaulted his wife and damaged a bathroom door inside the unit. The wife got a temporary restraining order against the husband and showed it to the landlord. The next day, for no apparent reason, the landlord served the wife with an eviction notice. All of the following statements are incorrect EXCEPT

- A. the wife may have a basis for a lawsuit against the landlord.
- B. the husband may have a basis for a lawsuit against the landlord.
- C. the husband could sue the landlord for breach of the warranty of habitability.
- D. the wife could sue the landlord for breach of the warranty of habitability.



# UNIT 6

## Property Valuation and Financial Analysis

### LEARNING OBJECTIVE

*When you have completed this unit, you will be able to accomplish the following.*

- ♣ Describe property valuation and financial analysis in California.

#### I. VALUE

An appraisal is an estimate or opinion of value supported by an analysis of relevant property data.

##### A. Market value

1. Market value is the highest probable price in terms of cash or its equivalent that a property will bring when
  - a. a willing seller would sell and a willing buyer would buy,
  - b. the property is exposed for a reasonable time,
  - c. both parties are familiar with the property's uses, and
  - d. neither is under abnormal pressure to sell or buy.

##### B. Market price

1. The actual price paid in a transaction; price may deviate from value

**C. Essential elements of value (DUST)—cost is NOT an element of value**

1. Demand
2. Utility
3. Scarcity
4. Transferability

**D. Forces influencing value**

1. Physical
2. Economic
3. Governmental
4. Social

**E. Subjective vs. objective value**

1. Subjective value—value in use
2. Objective value—value in exchange (market value)

**F. Principles of value**

1. Highest and best use occurs first in appraising vacant land, before analyzing comparative sales
2. Principle of substitution the most important principle in appraisal
3. Supply and demand
4. Anticipation—value can increase or decrease due to some future benefit or detriment that will affect the property
5. Conformity
6. Regression—value of overimproved property declines
7. Progression—value of underimproved property increases
8. Plottage—the increased value resulting from assemblage (act), combining adjacent lots into one larger lot
9. Balance—point of maximum productivity and maximum value is achieved when all factors of production (land, labor, capital, coordination) are in balance
10. Contribution—value of an improvement depends upon how much it adds or detracts from the overall value

## II. METHODS OF ESTIMATING VALUE/APPRaisal PROCESS

### A. Sales comparison approach/market approach/market data approach—primarily residential/vacant land

1. Property evaluating—subject
2. Similar properties recently sold—comparables or comps
3. Adjustments made to comparables
4. Comp better –, comp worse +
5. Competitive market analysis (CMA) uses similar approach but is not an appraisal
6. Whenever possible, property evaluated using comparison with recent sales
7. Sales comparison method is the best method to arrive at vacant land value

### B. Cost approach/replacement cost approach—most effective method for special purpose buildings or new construction

1. Estimate new construction cost
  - a. Reproduction cost new—exact replica
  - b. Replacement cost new—same function or utility
2. Methods of estimating cost of new construction
  - a. Quantity survey is a highly involved process of estimating cost of new construction by detailing raw material and installation costs; most difficult but most accurate method (rarely used)
  - b. Unit cost in place method estimates the installed price of components
  - c. Cubic foot or square foot method estimates cost based on the dimensions of the property (most commonly used)
  - d. Index method (least accurate)
3. Deduct for loss in value (depreciation)

**Figure 6.1: Deterioration vs. Obsolescence**

Physical Deterioration	Functional Obsolescence	Economic Obsolescence
■ Internal (inside the property lines)	■ Internal (inside the property lines)	■ External (outside the property lines)
■ Loss of value (dollar amount) associated with wear and tear	■ Loss of value (dollar amount) associated with design, layout, etc.	■ Loss of value (dollar amount) associated with forces outside the property lines
■ Curable ■ Incurable	■ Curable ■ Incurable	■ Incurable

4. Estimate and add in land value (using market approach)
5. Economic life = theoretical life
  - a. Time period from date of construction that the improvement will add value to the land
  - b. Frame house: 40–60 years
6. Effective age = how old the improvement appears to be
7. Actual or chronological age = how old it really is
8. Remaining economic life = time period from date of appraisal that the improvement will continue to add value to the land
9. Formula:
  - a. Economic life – effective age = remaining economic life
  - b. Remaining economic life = economic life – effective age

### C. Income approach—income-producing properties

1. Capitalization
2. Income = rate  $\times$  (times) value  
 $I = \text{net annual income}$ ,  $R = \text{cap rate}$ ,  $V = \text{value}$

$$\frac{\text{NOI}}{\text{Rate} \times \text{Value}}$$

3. Potential gross income
  - a. Contract (scheduled) rent
  - b. Market rent
    - vacancy and collection losses (percentage of potential gross)
    - effective gross income
    - operating expenses (do not include debt service)
    - net operating income (NOI)

4. Gross rent multiplier (alternative to capitalization that takes into account gross income but not expenses)

- a. Formulas:

annual gross rent multiplier  $\times$  annual gross rent = value

OR

monthly gross rent multiplier  $\times$  monthly gross rent = value

#### **D. Additional techniques/variations**

1. Development method—vacant land
2. Property residual technique is used in the income approach to estimate the total value of the property, including land and improvements

#### **E. Frontage/front foot/4-3-2-1 rule**

1. Frontage is the length of the property abutting a street.
2. Front foot is a measure of frontage used in appraising value of commercial property; each front foot is presumed to extend the depth of the lot.
3. The 4-3-2-1 rule is used for commercial property.

#### **F. Reconciliation process**

1. Final step in valuation process—appraiser analyzes and weighs estimates of value from market, cost, and income approaches
2. Arrives at final estimate of value; NOT an average of the value estimates

#### **G. A narrative report is the most comprehensive and longest type of appraisal report**

### **III. THE FINANCIAL INSTITUTIONS REFORM, RECOVERY, AND ENFORCEMENT ACT (FIRREA)**

#### **A. Appraisers must comply with Uniform Standards of Professional Appraisal Practice (USPAP)**

#### **B. California licensing requirements**

1. An appraiser with a residential license may appraise residential property (one to four units) up to a transaction value of \$1 million.
2. An appraiser who is a certified residential appraiser may appraise all residential and nonresidential property up to a transaction value of \$250,000.
3. An appraiser who is a certified general appraiser may perform all appraisals.

# UNIT 6 REVIEW QUESTIONS

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## True/False Questions

1. An appraisal is the appraiser's opinion of value as of a specified date.
  - A. True
  - B. False
2. A real estate licensee has the authority to complete an appraisal.
  - A. True
  - B. False
3. Market value is the most probable price a property would bring in an arm's length transaction.
  - A. True
  - B. False
4. Market price may deviate from market value.
  - A. True
  - B. False
5. The element of value utility answers the question, does the property fulfill a specific need?
  - A. True
  - B. False
6. Demand is determined by the finite supply of land.
  - A. True
  - B. False
7. Transferability is affected by the affordability of properties.
  - A. True
  - B. False
8. The highest and best use of real estate is always its present use.
  - A. True
  - B. False
9. Real estate values are driven by the anticipation of future benefits.
  - A. True
  - B. False
10. Price moves with supply; when supply goes up, prices go up.
  - A. True
  - B. False
11. Substitution is the basis of the cost approach.
  - A. True
  - B. False
12. Property of higher value tends to decrease in value when surrounded by properties of lower value.
  - A. True
  - B. False
13. Contribution determines the increasing or decreasing returns on improvements.
  - A. True
  - B. False
14. Increasing returns are improvements that add less value than they cost.
  - A. True
  - B. False
15. The first step in the appraisal process is to analyze the data.
  - A. True
  - B. False
16. There are four methods of estimating value.
  - A. True
  - B. False
17. The sales comparison approach is the most important method for appraising residential property.
  - A. True
  - B. False
18. The sales comparison approach is used on properties that exhibit a high degree of similarity.
  - A. True
  - B. False
19. Adjustments are made to the sales price of the subject property.
  - A. True
  - B. False

20. Comparables are similar properties that recently sold.

- True
- False

21. The cost approach is the most effective method for unique properties.

- True
- False

22. The formula for the cost approach is cost to build new minus accrued depreciation plus land value equals value.

- True
- False

23. Reproduction cost is the cost of a new building of exactly the same design and materials as the subject property.

- True
- False

24. Economic obsolescence is associated with wear and tear.

- True
- False

25. The income approach is used for properties that generate income.

- True
- False

26. In estimating value by the income approach, the appraiser first determines the property's potential gross income.

- True
- False

27. The capitalization rate is the property owner's effective gross income.

- True
- False

28. Debt service is needed to calculate net operating income.

- True
- False

29. Market rent is the rent received by the current property owner.

- True
- False

30. Contract rent is always lower than market rent.

- True
- False

31. Bad debt and vacancy losses are subtracted from gross income to derive effective gross income.

- True
- False

32. Operating expenses are subtracted from effective gross income to arrive at net operating income (NOI).

- True
- False

33. By applying a capitalization rate to net operating income, the appraiser arrives at an estimate of cash flow.

- True
- False

34. The cap rate is the property's estimated value.

- True
- False

35. Cap rate equals net operating income divided by market value.

- True
- False

36. The cap rate can be developed by analyzing historical rent data.

- True
- False

37. The better the investment the higher the cap rate.

- True
- False

38. Financing costs will vary depending on the individual property buyer's financial position and loan options available.

- True
- False

39. The gross multiplier is arrived at by dividing sales price by gross income.

- True
- False

40. Annual gross multiplier is more likely to be used for residential property.

- True
- False

41. Gross income times gross multiplier equals market value.

- True
- False

42. Frontage is the length of the property abutting a street.

- True
- False

### Multiple-Choice Questions

- Which of the following BEST explains the principle of progression?
  - A house of lesser value placed among homes of a greater value will further decrease its value.
  - A house of lesser value placed among houses of greater value will increase its value.
  - A house of greater value placed among homes of a lesser value will decrease its value.
  - A house of greater value placed among homes of a lesser value will increase its value.
- If effective demand for real estate in a given area remains the same, the market price
  - rises when supply increases.
  - lowers when supply decreases.
  - rises when supply decreases.
  - rises when supply remains the same.
- Cost is always a measure of the present worth of \_\_\_\_\_; maintenance cost is a \_\_\_\_\_; and value is a measure of \_\_\_\_\_.
  - past expenditure; past sacrifice; future income
  - past sacrifice; present expenditure; future income
  - present expenditure; past expenditure; present income
  - future sacrifice; present expenditure; present income
- Appraisers are often called upon to determine the appropriateness of an investment in relation to a particular site, furnishings in a particular building, or services rendered by a property management agency. This is an example of the appraisal principle of
  - surplus productivity.
  - supply and demand.
  - cost benefit analysis.
  - diminishing returns.
- The economic life of improved property is \_\_\_\_\_ in relation to the physical life of the property.
  - greater
  - lesser
  - the same
  - dependent on the type of improvement
- The principle of value that affirms that a purchaser will buy goods and services at the lowest cost available is
  - substitution.
  - regression.
  - inflation.
  - retribution.
- Where there is a high percentage of owner-occupied dwellings in a neighborhood with no turnover, there is (are) usually
  - high rents.
  - a low rate of turnover.
  - stabilized values.
  - a high cost of financing.
- Which of the following is NOT one of the four great forces that influence real estate value?
  - Social ideas and standards
  - Economic fluctuations
  - Government regulations
  - Private restrictions
- As a standard rule, as the depth of a lot increases to a depth greater than other lots in the area,
  - the front-foot value increases.
  - the square-foot value increases.
  - there is no difference in value.
  - the total value of the lot would be less.
- The period during which improvements contribute to the value of property is called
  - economic vitality.
  - economic life.
  - asset investment life.
  - accrued appreciation.
- Amenities of residential real estate are
  - related to its capacity to provide shelter effectively.
  - the property's physical attributes.
  - measurable on the market.
  - not considered by appraisers because they are intangible qualities.

12. Which would LEAST likely affect the stabilization of value on a single-family residence in a residential neighborhood?
  - A. Zoning
  - B. Private restrictions
  - C. Newness
  - D. Availability of public transportation
13. A roof that slopes upward from all four sides and is joined at the ridge is called
  - A. a gable roof.
  - B. a gambrel roof.
  - C. a hip roof.
  - D. a mansard roof.
14. An apartment house under construction has many prospective renters. The city now wants to widen the street. This change results in a 10% loss of renters. This loss would be an example of
  - A. economic obsolescence.
  - B. functional obsolescence.
  - C. physical obsolescence.
  - D. physical deterioration.
15. An appraiser using the land residual approach is attempting to determine
  - A. building value.
  - B. land value.
  - C. capitalization rate.
  - D. income.
16. If a capitalization rate increases, then the value of property will
  - A. increase.
  - B. decrease.
  - C. stay the same.
  - D. none of these.
17. Land value should ALWAYS be determined on the basis of
  - A. capitalization of future income.
  - B. selling prices of comparable parcels.
  - C. utility value.
  - D. economic life.
18. What is the basic principle supporting the comparative analysis appraisal method?
  - A. Principle of substitution
  - B. Principle of integration and disintegration
  - C. Principle of highest and best use
  - D. Principle of change
19. Which of the following would NOT contribute to obsolescence?
  - A. Misplaced improvements
  - B. Change in directional growth pattern
  - C. Normal wear and tear due to use
  - D. Massive cornices on an apartment building
20. The easiest way for an appraiser to calculate the present value of industrial land is with
  - A. a quantity survey.
  - B. market data.
  - C. the unit-in-place cost method.
  - D. a review of the building permit records.
21. The MOST frequently used method of land or site valuation is
  - A. residual.
  - B. developmental.
  - C. market.
  - D. abstract.
22. The maximum possible income an income property can yield is
  - A. effective gross income.
  - B. gross scheduled income.
  - C. net income.
  - D. net spendable income.
23. In the narrative form of appraisal report, where would the property value be stated?
  - A. Description of use
  - B. Description of the neighborhood
  - C. Legal description of the property
  - D. Purpose of the appraisal
24. When comparing physical life to economic life, the economic life usually
  - A. is the same.
  - B. is greater.
  - C. is lesser.
  - D. depends on the improvement.
25. All these statements about depreciation are true EXCEPT
  - A. it always is concerned with intrinsic factors but never with extraneous factors.
  - B. it is a loss of value from any cause.
  - C. it can be a loss of value due to wear and tear.
  - D. it includes all influences that reduce the value of property below replacement cost.

26. These paragraph headings—Introduction, Description of General Neighborhood, Market Value & Economic Factors, and Final Estimate of Value—would be present in which type of appraisal?

- Form (summary)
- Letter (restricted)
- Narrative (self-contained or summary)
- None of these

27. An owner has a 100-unit apartment house. Which item would be deductible from the gross income in determining net operating income?

- Depreciation
- Income tax
- Wages for part-time gardeners and maintenance personnel
- Mortgage payments of principal and interest

28. In establishing an estimate of value by appraisal, it is very important to differentiate between the purpose of the appraisal and

- the principles of appraisal.
- the amenities to the owner.
- the appraisal process.
- the function for which the appraisal is being made.

29. On hot days, customers prefer to walk in the shade. Certain locations, due to the sun's fading effect on display window clothing, are the least desirable. Which is the LEAST desirable side of the street for a clothing retailer?

- Southwest
- Southeast
- Northwest
- Northeast

30. The BEST definition of capitalization is

- the highest rate of return on an investment.
- the minimum rate of return on an investment.
- the relationship between value and net worth.
- the result of dividing net income by a percentage rate of return to determine value.

31. Which criterion would NOT be used to determine net income for an income property?

- Vacancies
- Mortgage interest
- Management fees
- Maintenance costs

32. Smith built a \$250,000 house in a neighborhood in which houses are valued between \$75,000 and \$85,000. Any resulting loss of value would be an example of

- physical depreciation.
- functional obsolescence.
- physical obsolescence.
- economic and functional obsolescence.

33. In order to arrive at an effective gross income for rental properties, an appraiser should deduct what from gross income?

- Vacancies and collection losses
- Real property taxes
- Repairs
- Depreciation

34. If an appraiser does not adhere to appraisal standards (*USPAP*) for the purpose of defrauding an Federal Deposit Insurance Corporation-insured lender, the appraiser could be guilty of

- a misdemeanor.
- a felony.
- violating Department of Real Estate rules and regulations.
- an ethics violation.

35. What is the first step in the appraisal process?

- Make a preliminary survey and appraisal plan.
- Classify the data.
- Define the appraisal problem.
- Organize the data program.

36. Of the four appraisal terms listed, which has the LEAST relation to the others?

- Sales
- Comparative
- Comparable
- Reconciliation

37. When applied as a deduction from gross income, the vacancy factor is known to

- be constant.
- generally discourage prospective purchasers.
- vary both in locality and from time to time.
- be impossible for the appraiser to estimate with any accuracy.

38. In arriving at an estimate of value based on selling prices, the appraiser is MOST interested in the date

- the deed was recorded.
- the sale went into escrow.
- the deed was signed.
- the buyer and the seller agreed on the price.

39. An appraiser is called upon to appraise a property on which there is a building of no value. The appraiser should

- ignore the building.
- add the salvage value of the building.
- appraise for highest and best use and disregard the cost of demolition.
- appraise for highest and best use and deduct the cost of demolition.

40. What is the BEST definition of *economic rent*?

- Payment for use of property designated in a lease
- The amounts the owner actually receives in rents
- The amount left after the lessor pays expenses
- The amount the property would rent for if it was available in today's market

41. In planning a shopping center in a suburban community, which would be the MOST important consideration?

- Proximity of shipping and warehousing facilities
- Purchasing power
- Amenities
- Weather

42. An apartment was purchased by a buyer who gave a \$30,000 cash down payment, assumed a \$60,000 first trust deed, and agreed to pay \$2,400 for delinquent real property taxes. The buyer also agreed to pay 50% of the broker's 5% commission and \$1,150 for closing costs. For tax purposes, the buyer's basis will be MOST nearly

- \$90,000.
- \$92,400.
- \$95,800.
- none of these.

43. An increase in the appraised value of property, which is considered unearned increment, would MOST probably result from

- capital improvements.
- management expense.
- increase in amenities.
- increase in population.

44. The amount an appraiser charges for an appraisal is established by

- the Federal Housing Authority.
- the real estate commissioner.
- the Office of Real Estate Appraisers.
- the agreement between the appraiser and the client.

45. The standards that a state-licensed or state-certified appraiser must follow are found in

- the URAR.
- the *USPAP*.
- the MAI.
- the NAR.

46. A fee appraiser

- assesses land for the government.
- is a self-employed appraiser who, for a fee, appraises property.
- works full time for a broker.
- works full time for a lender.

47. Smith owns an older apartment building and is considering the merits of an expensive remodeling plan. The deciding factor that would be instrumental on his final decision would be

- the effect of the plan on the net income.
- the cost of the plan.
- the wishes of the tenants.
- the potential increases in the real property taxes.



# UNIT 7

## Transfer of Property

### LEARNING OBJECTIVE

*When you have completed this unit, you will be able to accomplish the following.*

- ♣ Describe the transfer of property in California.

#### I. ALIENATION

##### A. Alienating property

1. *Alienating property* means conveying property—the opposite of acquisition
2. Can be voluntary or involuntary

##### B. Types of deeds

Every deed conveys whatever interest is held by the grantor, unless it specifically states that it is conveying a lesser interest. The major difference between types of deeds lies in the extent of the promises given by the grantor to the grantee.

1. Grant deed—most common
2. Quitclaim deed
3. Warranty deed—has five covenants and a guarantee of title (seldom used in California because of prevalence of title insurance)
4. Gift deed—given in return for love and affection
5. Involuntary deed—must be recorded to be effective

**C. Essential elements of a valid deed**

1. In writing
2. Signed by grantor
3. Competent grantor
4. Granting clause (words of conveyance)
5. Adequate description of property
6. Must designate a grantee

Not required: date, signature of grantee, and legal description

**D. Essentials for a valid transfer**

1. Valid deed
2. Delivered—must pass out of control of grantor during grantor's lifetime; controlled by the intention of the grantor to convey property
3. Accepted by grantee(s)—evidenced by possession of deed, encumbering title, or any act demonstrating ownership, such as taking possession

**E. Conveyance after death**

1. *Probate* is the judicial process to prove or confirm validity of a will, collect assets, pay debts and taxes, and distribute all of a deceased's assets.
2. *Devise* is the act of transferring a deceased's (called the *devisor* or *testator*) interest in real estate to another (*devisee*) by will.
3. If intestate, laws of descent and intestate succession determine heirs/descendants.
4. Court determines broker's commission if a property is sold through probate.

**F. Involuntary alienation**

1. Adverse possession is ownership granted by the courts due to actual, open, continuous, hostile, notorious, and exclusive possession of another's land for five years under claim of right or color of title. Taxes must be paid for five years.
2. Easement by prescription is an easement gained through adverse possession. It terminates due to nonuse after five years.
3. *Easement by necessity* is an easement created by law to prevent landlocked property. The grantee receives an easement over the grantor's land but only if there is no other access to the grantee's land.

**G. Public transfer**

1. The state transfers ownership to a private party by land patent or patent deed.
2. A conveyance of property from a private party to the state is a dedication.

#### **H. Recording**

1. Generally not required for validity (although involuntary transfers require recording to be effective)
2. Gives constructive (legal) notice to protect interests (taking possession also gives constructive notice)
3. Can determine priority (first in time, without notice is first in right)
4. Record in the county where property is located

### **II. TITLE INSURANCE**

#### **A. Buyer's goal is to obtain marketable (merchantable) title**

#### **B. Title insurance**

1. The examiner checks the abstract of title for history of conveyances and traces the chain of title.
2. The certificate of title lists current title status and encumbrances, and certifies that the records are accurate as recorded.
3. A preliminary report is an offer to issue a policy based on the conditions of the report.
4. Types of policies are the following:
  - a. Standard (CLTA) matters discoverable in the public record (e.g., improper delivery)
  - b. Extended policy (ALTA) matters that would not be revealed by an inspection of the public records (e.g., unrecorded easements)
5. Zoning ordinances are not insurable.
6. The premium is paid once, at the time the policy is issued.

### **III. ESCROW/SETTLEMENT/CLOSING**

#### **A. Escrow/settlement procedures**

1. *Escrow* or *settlement* is the means by which parties to a contract carry out the terms of an agreement.
2. Parties appoint a third party to act as a depository, agent, or neutral third party.
3. The seller's deed and the buyer's money are deposited with an escrow agent according to an escrow agreement that sets forth conditions to be met before the sale will be consummated.
4. Once in escrow, funds can be released upon written instructions of both parties (mutual release papers), through court action (interpleader), or through a binding arbitration decision.
5. If the purchase agreement and the escrow instructions disagree, escrow instructions would prevail because they would be the later contract.
6. During escrow, the escrow agent is typically viewed as being a dual agent, representing both parties in the transaction. Once the transaction closes, the escrow agent may become the single agent of either party for any remaining issues pertaining to the parties.
7. The escrow agent collects reports required for the transaction.
8. A *complete escrow* is where all instructions have been completed, but the transaction has not yet closed.

### B. Closing statement—debits and credits

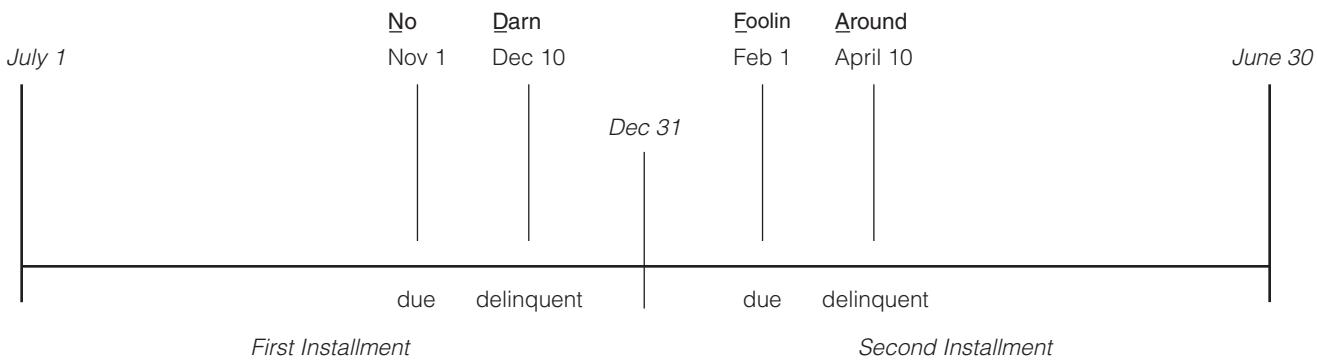
1. *Credit to seller* is anything that increases the amount of money the seller takes from the closing.
  - a. Examples: sale price, prepaid taxes
2. *Debit to seller* is anything that decreases the amount of money the seller takes from the closing.
  - a. Examples: brokerage fee, mortgage payoff
3. *Credit to buyer* is anything that decreases the amount of money the buyer must bring to the closing.
  - a. Examples: earnest money, new mortgage
4. *Debit to buyer* is anything that increases the amount of money the buyer must bring to the closing.
  - a. Examples: sale price, discount points (if paid by buyer)
5. Proration is based on a 360-day year (30-day months). Rent is paid in advance; mortgage interest is paid in arrears.
6. Insurance may be short rated—when the policy is canceled before its expiration.

## IV. TAX ASPECTS

### A. Property taxes—at value—ad valorem

1. The assessment roll establishes the tax base.
2. Properties can be reassessed for current value and improvements. Reassessments can be appealed to an assessor's appeals board.
3. The fiscal year for property taxes begins on July 1. (See Figure 7.1.)
  - a. The first installment, covering July 1–December 31, is due November 1.
  - b. The second installment, covering January 1–June 30, is due February 1.

**Figure 7.1: Fiscal Tax Calendar**



**B. Special assessments**

1. Taxes charged against specific properties that benefit from a public improvement
2. Paid along with property taxes and enforced by a lien

**C. Mello-Roos Community Facilities Act of 1982**

1. Created a special form of property assessment involving an improvement bond; may or may not appear on property tax bill
2. Seller of a one- to four-unit dwelling must disclose if property is subject to a Mello-Roos lien

**D. Documentary transfer tax**

1. City or county tax rate of \$.55 per \$500 or fraction thereof of purchase price minus existing loans transferred

**E. Depreciation**

1. For tax purposes, non-owner-occupied residential properties can be depreciated over 27½ years.
2. Nonresidential (commercial, industrial) properties can be depreciated over 39 years.
3. Only improvements are depreciated—never land.

**F. Capital gains exemption for principal residence**

1. No tax on the first \$250,000 of profit (single) or \$500,000 of profit (married) from the sale of principal residence
2. Must reside in residence two out of the last five years
3. Exemption can be taken every two years (once-in-a-lifetime limit no longer exists)

**G. Successor's liability**

1. The purchaser of a business may have successor's liability if the sales taxes have not been fully paid by the seller.
2. The purchaser should get a certificate of clearance from the Board of Equalization showing that the seller has paid all sales taxes due.

**H. Tax shelters**

1. Associated with income taxes

# UNIT 7 REVIEW QUESTIONS

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## True/False Questions

1. Chain of title is a history of errors found in the title search.
  - A. True
  - B. False
2. If errors or missing documents are found in a title search, then the title is clouded.
  - A. True
  - B. False
3. The California Land Title Association (CLTA) or standard policy is also called the lender's policy.
  - A. True
  - B. False
4. The American Land Title Association (ALTA) policy lasts as long as the loan is in place.
  - A. True
  - B. False
5. A grant deed has no implied warranties.
  - A. True
  - B. False
6. For a valid deed to be effective and transfer title, it must be recorded.
  - A. True
  - B. False
7. A warranty deed is commonly used to clear clouds on title.
  - A. True
  - B. False
8. Escrows are only used when dealing with real property.
  - A. True
  - B. False
9. The escrow agent is given written escrow instructions to carry out the terms of the contract that is the basis of the transaction.
  - A. True
  - B. False
10. If a conflict arises between the parties to the contract, the escrow holder can bring legal action known as interpleader.
  - A. True
  - B. False
11. Either party, buyer or seller, can unilaterally cancel the escrow.
  - A. True
  - B. False
12. Proposition 13 sets the maximum annual tax on real property to 2% of base year value.
  - A. True
  - B. False
13. Assessed value remains the same for the life of the property.
  - A. True
  - B. False
14. The fiscal tax calendar year begins on July 1.
  - A. True
  - B. False
15. Special assessments can be imposed on real property for a specific local purpose, such as a street construction or repair.
  - A. True
  - B. False
16. The documentary tax rate is \$1.10 per \$500 or fraction of \$500 of the sales price.
  - A. True
  - B. False
17. A special form of property assessment was created by the Mello-Roos Community Facilities Act.
  - A. True
  - B. False
18. An owner-occupied residence qualifies for a homeowner's exemption of the first \$4,000 of full cash value.
  - A. True
  - B. False

19. Probate is the name of the court process that proves or confirms validity of a will.  
A. True  
B. False

20. Bequest is the act of transferring a deceased's interest in personal property by will.  
A. True  
B. False

21. The broker determines the commission if a property is sold through probate.  
A. True  
B. False

22. Ownership in severalty is made up of multiple owners.  
A. True  
B. False

23. Tenants in common may own unequal shares.  
A. True  
B. False

24. Joint tenants benefit from right of survivorship.  
A. True  
B. False

### Multiple-Choice Questions

1. Mr. Kale wants to purchase a mountain lot from an owner on which a final report has not been issued by the real estate commissioner. He is concerned about a possible blanket encumbrance, deed restrictions, utility easements, who is responsible for street maintenance, financing, et cetera. The BEST single source to find the answers to these questions would be  
A. the county planning commission.  
B. the real estate commissioner.  
C. the county engineer.  
D. the local title company.
2. Most buyers elect which type of title insurance policies?  
A. Standard coverage  
B. Extended coverage  
C. ATA  
D. ALTA
3. A title insurance company will insure  
A. the validity of the tenant's lease, free of liens and encumbrances.  
B. the validity of an easement.  
C. losses from undesirable restrictions in a grant deed.  
D. all of these.
4. A buyer acquires an interest in real property by a grant deed and obtains a standard policy of title insurance on the property. Which of the following is warranted by the grantor?  
A. That the grantor is capable of passing title  
B. That there is no forgery in the chain of title  
C. That the grantor is the owner of the property  
D. That there are no undisclosed lien claims against the property that have been incurred by the grantor
5. A summary and digest of all transfers, conveyances, legal proceedings, and any other facts relied on as evidence of title, showing continuity of ownership, together with any other elements of record which impair title, is a definition of  
A. a certificate of title.  
B. an abstract of title.  
C. a chain of title.  
D. a boilerplate form.
6. What is MOST frequently employed to ensure title to real property for a grantee?  
A. Certificate of title  
B. Title insurance  
C. Recordation of deed  
D. Warranty deed
7. Recording a deed would give  
A. constructive notice.  
B. right of possession.  
C. actual notice.  
D. effective notice.
8. The effective delivery of a deed under law is dependent on  
A. recordation.  
B. acknowledgment by the grantor.  
C. intention of grantor.  
D. grantee having knowledge of its existence.

9. Martin purchased a lot from Brown and received a grant deed but did not record it. Brown then sold for value and deeded the same property to Williams, who, having no knowledge of the previous transaction, recorded the deed. Under these circumstances, Martin's deed was
  - A. void.
  - B. valid as to Williams's recorded deed but void as to subsequent recorded interests.
  - C. valid and effective.
  - D. void as to Williams's recorded deed.
10. Smith executes a deed to Brown and it is recorded. Brown is in possession. Later, Smith wants to set aside the conveyance claiming the deed was never delivered. Why will Smith probably be unsuccessful in the attempt to have it set aside?
  - A. Brown has possession of the property.
  - B. The deed is valid without recording.
  - C. The precedence of liens is established by recording.
  - D. Recording a deed raises the presumption of delivery.
11. A quitclaim deed releases present claim, rights, and title of
  - A. the grantor.
  - B. the grantee.
  - C. the servient tenement.
  - D. the property.
12. A deed made and delivered, but NOT recorded, is
  - A. invalid as between the parties and valid as to third parties with constructive notice.
  - B. valid as between the parties and valid as to subsequent recorded interests.
  - C. valid as between the parties and invalid as to subsequent recorded interests without notice.
  - D. invalid as between the parties.
13. To alienate title to real property, an individual
  - A. secures an ALTA policy of title insurance.
  - B. conveys title.
  - C. clouds a title.
  - D. records a homestead.
14. Alienation expresses a meaning MOST nearly opposite to
  - A. acquisition.
  - B. ad valorem.
  - C. acceleration.
  - D. amortization.
15. The real property taxes for the current fiscal tax year had been paid and amount to \$1,380. The property was sold and the escrow closed on May 1. How much did the buyer have to pay in escrow?
  - A. \$230
  - B. \$250
  - C. \$270
  - D. None of these
16. Which statement is TRUE with regard to escrow procedure?
  - A. A broker can hold an escrow account for compensation for other parties when he has no interest in the transaction.
  - B. When the escrow holder is in possession of a binding contract between the buyer and the seller, it is considered a complete escrow.
  - C. When the escrow requirements have been met, the escrow agency changes from a dual agency to a separate agency.
  - D. The escrow officer acts as an arbitrator of arguments between the buyer and the seller.
17. The primary responsibility for reporting a real estate transaction to the IRS is on
  - A. the lender.
  - B. the appraiser.
  - C. the real estate agent.
  - D. the escrow company.
18. An escrow closing statement that refers to recurring costs could be describing
  - A. deed transfer taxes.
  - B. title insurance.
  - C. impound accounts for taxes and insurance.
  - D. escrow charges.
19. What would appear as a credit to the seller on a closing statement?
  - A. Cash charge for recording buyer's deed
  - B. Proration of prepaid taxes
  - C. Proration of prepaid rents
  - D. Cash charge for a quitclaim deed
20. Escrow companies are subject to the corporations commissioner's regulations. Who would NOT be exempt?
  - A. Attorney-at-law
  - B. Broker not accepting a fee and handling his own escrow
  - C. Broker escrowing property of other brokers
  - D. Broker accepting a fee and handling his own escrow

21. An escrow company can

- request funding of the buyer's loan.
- order a termite report and authorize the work to be done.
- change the amount of the broker's commission.
- tell the buyers where to obtain the best available financing.

22. Which item would MOST likely be short-rated in escrow?

- Trust deed
- Real estate taxes
- Insurance
- Interest

23. What is usually referred to as a tax-free exchange generally means that there will be

- no taxes.
- an even exchange.
- no gain.
- deferred taxes.

24. In the sale of a business, sales tax would be paid on

- inventory of goods on hand.
- goodwill.
- trade fixtures and furniture.
- accounts receivable.

25. A buyer purchased a property from the seller on August 15, 2014. The buyer was to take possession as of September 30, 2014, with all prorations to be as of the same date. On November 1, 2013, the seller had paid the taxes for the fiscal year of 2013-2014. The escrow closing statement would show

- buyer pays seller for three months' taxes.
- buyer pays seller for nine months' taxes.
- seller pays buyer for nine months' taxes.
- seller pays buyer for three months' taxes.

26. For federal income tax purposes, a taxpayer could adjust the cost basis of the personal residence on income tax records for which item?

- The addition of a concrete patio
- Depreciation
- Interest on a loan
- Fire insurance premiums paid

27. What is NOT a method for providing for depreciation?

- Straight line
- Sinking fund
- Obsolescence
- Sum-of-the-years' digits

28. What BEST defines adjusted basis of a property for income tax purposes?

- Acquisition cost
- Acquisition cost plus capital improvements
- Acquisition cost plus capital improvements plus depreciation
- Acquisition cost plus capital improvements minus depreciation

29. Smith buys an apartment building for \$100,000. He keeps it for 10 years and sells it for \$100,000. He had depreciated the improvements \$40,000 over his period of ownership. As to his income tax position,

- he has no recognized gain.
- his gain is taxable as ordinary income.
- he has to pay capital gains on the amount of the depreciation.
- his gain may be deferred.

30. The county maintains an assessment roll that includes the assessed value of property. The purpose of this assessment roll is

- establishment of the tax amount.
- establishment of the assessment for the tax base.
- equalizing of assessments.
- setting of the tax rate.

31. Points paid in obtaining a loan are treated in what manner on the federal income tax return?

- The manner in which they are treated depends on what they are being used for.
- Points are always deductible.
- Points are deductible only if the loan is obtained through a state or federal bank.
- Points are always deductible if used for interest but not for specific services by a lender.

32. What is an example of boot received for income tax purposes?

- Increase in depreciation taken
- Decrease in depreciation
- Net debt relief in a tax-deferred exchange
- All of these

33. Which statement regarding a tax-free exchange is TRUE?

- To be eligible, a property must be held for income or investment or for use in trade or business.
- Each party must trade for like property of equal value with a smaller mortgage and receive boot.
- A party to the exchange can deduct a loss on the exchange.
- A rented house cannot be exchanged for an office building.

34. A capital gain exclusion on a principal residence is

- \$250,000.
- \$250,000 for an individual or \$500,000 for a married couple every two out of the last five years.
- \$250,000 for an individual or \$500,000 for a married couple, once in a lifetime.
- \$250,000 for an individual or \$500,000 for a married couple, once in a lifetime if one of them is over 55 years of age.

35. Smith buys an apartment building for \$300,000. She keeps it for 10 years and sells it for \$300,000 because the land and the building value did not increase. She had depreciated \$110,000 over her period of ownership. As to her tax position,

- she has no recognized gain.
- her gain is taxable as ordinary income.
- her gain may be deferred.
- she has to pay capital gains on the amount of the depreciation.

36. Smith sold a house under an installment sales agreement. The main advantage of this method is the ability to

- choose which years in which to declare the gain.
- postpone declaring the gain until the debt is fully repaid.
- prorate the gain over the term of the installment contract.
- declare the gain in the year of sale.

37. A property is sold under an installment sales contract that the vendee recorded. Later, the vendee defaults without executing a release document. The vendor, to remove the cloud from his title, may

- petition the county recorder to remove all evidence of the documents from the records.
- bring a quiet title action in court.
- execute a quitclaim deed.
- do none of these.

38. Which of the following is a definition of a quiet title action?

- Procedure through court action to remove a cloud on title
- The result of a "dummy" transaction
- Foreclosure
- Quitclaim

39. A purchaser of real property who does not examine the public records on the property is still considered to have

- inquisitive notice.
- lack of notice.
- constructive notice.
- actual notice.

40. An interest in real property can be acquired through adverse possession or by prescription. The interest acquired by prescription is

- equitable title.
- legal title.
- by private grant.
- a right to use another's land.

41. All the elements for acquiring title to real property by adverse possession are necessary for acquiring an easement by prescription EXCEPT

- open and notorious use.
- hostile to true owner.
- payment of taxes.
- a claim of prior right.

42. A purchases a home and owned it in fee. Later, A sold the home on a land contract to B. Now A wishes to sell the contract to C. In order to do this, A must

- transfer title to C if assigning the contract.
- assign the contract to C if transferring title.
- obtain the vendee's permission, if the contract is unrecorded, to create a new encumbrance if the payments on the existing encumbrance and the new encumbrance will exceed the payment on the contract.
- do all of these.

43. All these instruments are used to transfer an interest in real property EXCEPT

- a bill of sale.
- a trust deed.
- a mortgage.
- an agreement of sale.

44. The requisites of a grant deed differ from those of a land contract in which way?

- Warranties to purchaser
- Signature of principals
- Designation of price
- All of these

45. A buyer of a piece of property fails to examine public records on the property. The buyer is considered to have

- actual notice.
- constructive notice.
- assumed notice.
- conditional notice.

46. In the absence of a special agreement to the contrary, a trust deed normally having highest priority is one that was

- recorded first.
- executed first.
- a construction mortgage.
- executed and delivered first.

47. If a married person dies intestate, separate property owned by the decedent is divided

- one-third to the surviving spouse and two-thirds to the surviving children if there is more than one child.
- one-half to the surviving spouse and one-half to the children.
- equally between the surviving spouse and the children.
- in none of these ways.

48. An executrix is

- named by the attorney handling the probate.
- named in the will of the decedent.
- appointed by the court.
- chosen by the heirs to represent them.

49. Carson acquired title to several properties before his arrest. While in prison, he wanted to convey one property to his son and sell another. How would being in prison affect his ability to convey?

- It would be hard to acquire title insurance.
- He must first get permission from the California Adult Authority.
- He can dispose of his property as he pleases.
- His conveyance must be approved by an officer of the Department of Corrections.

50. Escrow recently closed on four different properties. Which vesting shows an estate in severalty?

- "Jorge Hernandez, Emma Roberts, and Sarah Nguyen, as Joint Tenants"
- "Ann Sanders, Elise Thibaux, and Jim Williams, as Tenants in Common"
- "Diana Lim, a Single Woman"
- "Albert Sinclair and Janet Sinclair, Husband and Wife, as Community Property with Right of Survivorship"

51. Ann, Ben, Cam, and Dan, four unrelated friends, purchased a home together. They are holding title as joint tenants. Ann adopts a child and executes a will so that, in the event she dies, her interest in the home goes to the child. Before any change can be made to the vesting, Ann dies. What will happen to Ann's interest in the home?

- Ann's interest in the home will go to the surviving joint tenants.
- Ann's interest in the home will go to the child.
- Half of Ann's interest will go to the surviving joint tenants, and half will go to the child.
- The laws of intestate succession will govern the disposition of Ann's interest in the home.



# UNIT 8

## Broker Only

**NOTE:** This unit is Broker content only. It is a self-study unit. Work through the exercises on your own and check your work in the Answer Key.

### PROPERTY OWNERSHIP AND LAND USE CONTROLS AND REGULATIONS

#### True/False Questions

1. Personal property can become real property and vice versa.
  - A. True
  - B. False
2. Air rights in land include minerals, oil, and gas.
  - A. True
  - B. False
3. A fixture is anything that is attached or affixed to land.
  - A. True
  - B. False
4. An encroachment is a revocable permission to use the land of another.
  - A. True
  - B. False
5. A fee simple defeasible estate lasts forever.
  - A. True
  - B. False
6. If the right of possession returns to the original property owner when a life estate ends, the original owner has a reversion.
  - A. True
  - B. False
7. In a metes-and-bounds property description, metes refer to boundaries and bounds to distances.
  - A. True
  - B. False
8. In a condemnation process of eminent domain, the property owner receives no compensation.
  - A. True
  - B. False
9. The government right of escheat applies when a property owner dies intestate and without any heirs.
  - A. True
  - B. False
10. Downzoning is a zoning change from dense to less-dense usage.
  - A. True
  - B. False

11. The disclosures required for lead-based paint only apply to target housing built before 1978.
  - A. True
  - B. False
12. A deed restriction is a prohibition against a property use that is imposed in the grantee's deed.
  - A. True
  - B. False
13. Owners of riparian water rights own the water.
  - A. True
  - B. False
14. Littoral rights belong to owners of land bordering a still body of water, such as a lake.
  - A. True
  - B. False
15. Stock cooperative owners receive a deed and a separate property tax bill.
  - A. True
  - B. False

### Multiple-Choice Questions

1. A seller of a parcel of improved real estate excludes certain items from the purchase agreement. Which of the following choices did NOT need to appear on that list of exclusions?
  - A. The 1,000-pound grand piano situated in the living room
  - B. The 100-year-old antique chandelier hanging in the dining room
  - C. The ripe grapes growing in the vineyard
  - D. The installed Italian marble fireplace mantel
2. In an all-cash deal, Sarah Joy and Aiko Tanaka purchased a large parcel of real estate in a rural area. They bought the realty from an old college friend, who conveyed the property to them using a quitclaim deed. Escrow was not used for the transaction. Neither the seller nor the buyers purchased an owners' policy of title insurance. After the purchase transaction was completed, Joy and Tanaka discovered that the property was landlocked. The seller said she had verbal permission to cross a neighbor's land to get to the road, but that had never been formalized in any kind of a written document. The neighbor now refused to grant the same license to Joy and Tanaka. Which of the following features of this transaction were illegal?
  - A. It was illegal to purchase real estate without buying an owners' policy of title insurance.
  - B. It was illegal to sell landlocked property and complete a purchase transaction of real estate without an escrow.
  - C. It was illegal for the neighbor to revoke the license allowing access to the street.
  - D. None of these activities are illegal.
3. For which of the following is there a split between legal title and equitable title?
  - A. A deed of trust
  - B. A living revocable trust
  - C. A land contract
  - D. All of these
4. As described by the rectangular survey system, a buyer purchased an entire section of land. How large was this property, and how many acres did it contain?
  - A. One-half square mile, containing 320 acres
  - B. One square mile, containing 640 acres
  - C. One-fourth square mile, containing 160 acres
  - D. 5,280 feet, with 40 acres

5. A single-family residence has been sold at a foreclosure for \$500,000. The foreclosing lien, dated and recorded in November 2019, had an outstanding balance of \$600,000. There is also a mechanic's lien for unpaid labor performed in October 2019, a lien that recorded in December 2019. Which of the following choices shows the correct order that the liens will be paid from the foreclosure proceedings?

- A. Special assessments before property taxes
- B. The mechanic's lien before the foreclosing trust deed
- C. The foreclosing trust deed before special assessments
- D. The foreclosing trust deed before property taxes

6. A single-family residence was constructed in 1962. The current owner is not a real estate licensee. The owner suspects, but does not have actual knowledge, that there is lead-based paint in the residence. In a recent lease transaction, the owner worked with a real estate broker and the appropriate lead-based paint warnings were signed in a timely manner by all appropriate parties. However, the real estate broker did not advise the owner to provide a 10-day opportunity to test for lead-based paint, and the owner did not do so. By failing to provide a 10-day opportunity to test for lead-based paint, the owner

- A. will be disciplined by the DRE for violating the federal lead-based paint law.
- B. did not violate the federal lead-based paint law.
- C. did not violate the law because there was no actual knowledge of lead-based paint.
- D. can sue the real estate broker for failing to provide adequate advice on lead-based paint testing.

## CONTRACTS

### True/False Questions

1. An unenforceable contract appears to be valid but may be disavowed by one or more parties.
  - A. True
  - B. False
2. An emancipated minor may not legally enter into a contract.
  - A. True
  - B. False
3. Under a net listing, the agent's commission is all money received for a property over a net amount set in the listing.
  - A. True
  - B. False
4. In an option listing, the broker takes a listing combined with an option to purchase, placing the broker in the dual role of agent and principal.
  - A. True
  - B. False
5. Caveat emptor (let the buyer beware) is the current precept of business.
  - A. True
  - B. False
6. The *Easton v. Strassburger* case applies to residential as well as commercial property.
  - A. True
  - B. False
7. The offer becomes an executory contract upon communication of acceptance.
  - A. True
  - B. False
8. Either party can change the offer terms by creating a brand new offer that replaces the original offer.
  - A. True
  - B. False
9. Loans with a due-on-sale clause can be assumed.
  - A. True
  - B. False
10. Usury is charging a rate of interest greater than allowed by law.
  - A. True
  - B. False
11. The right to buy property at some time in the future at an agreed-on price is called an exchange.
  - A. True
  - B. False
12. Advance fees are not trust funds.
  - A. True
  - B. False

**Multiple-Choice Questions**

1. On Monday, an owner of a commercial office building received an attractive offer from a prospective buyer. The owner hadn't listed or even considered selling the property, but the offer made the owner reconsider. Several days went by, and the owner told several friends about the high offer, and the owner's plans to accept it. Several people advised accepting the offer as quickly as possible. Unfortunately, the prospective buyer died on Saturday, prior to the owner communicating acceptance. What is the status of the offer?
  - A. The offer terminated upon the death of the prospective buyer.
  - B. The offer was invalid because the property was not listed for sale.
  - C. The judge can accept the offer when the will of the prospective buyer is probated.
  - D. The owner's friends can save the offer through sworn testimony related to the owner's intent to accept
2. An owner of a retail property is negotiating a lease with a tenant. The subject property is situated in an affluent area and is readily accessible from nearby freeways. The owner recently remodeled the building so that it has upscale amenities throughout, reflecting current market trends. Given the desirability of this property, what type of lease will benefit the landlord the MOST?
  - A. Land lease
  - B. Net lease
  - C. Gross lease
  - D. Double net lease
3. A seller listed a parcel of vacant land for \$2 million dollars. A buyer made an offer of \$2.5 million dollars, and the seller communicated acceptance. The purchase and sale contract was properly signed by both parties, and escrow was opened at a nearby escrow company. After the seller communicated acceptance, the buyer wired a \$20,000 earnest money deposit directly to escrow. What was the buyer's consideration?
  - A. The \$20,000 wired to escrow
  - B. The \$500,000 over the list price
  - C. The promise to pay the purchase price
  - D. The contractual element of consideration to be met when the buyer pays the purchase price
4. In California, which of the following parties can collect an advance fee for loan modification or loan forbearance work?
  - A. An attorney
  - B. A real estate broker
  - C. A real estate broker with a mortgage loan originator endorsement
  - D. None of these

## FINANCING

### True/False Questions

1. The Federal Reserve Bank is the central bank of the United States.
  - A. True
  - B. False
2. In a fully amortized loan, the entire amount of principal is due at the end of the loan term.
  - A. True
  - B. False
3. Commercial banks, savings and loan associations, and credit unions are all part of what is called the secondary mortgage market.
  - A. True
  - B. False
4. VA loans are available with no down payment to those men and women who served in the U.S. armed forces and were other than dishonorably discharged and to their spouses.
  - A. True
  - B. False
5. In a mortgage, the lender is the mortgagor.
  - A. True
  - B. False
6. The Real Estate Settlement Procedures Act prohibits kickbacks.
  - A. True
  - B. False
7. According to TRID (TILA-RESPA Integrated Disclosure Rule), the lender must provide the consumer with a Closing Disclosure with three business days of the receipt of the consumer's loan application.
  - A. True
  - B. False
8. A loan broker, which is typically a middleman between a lender and a borrower, cannot lend his own funds.
  - A. True
  - B. False

9. The SAFE Act (Secure and Fair Enforcement for Mortgage Licensing) is a federal law that provides for the licensing and registration of mortgage loan originators.
  - A. True
  - B. False

### Multiple-Choice Questions

1. A corporate employer promoted Elena Salazar to a management position in California. Salazar sold her home in New York and purchased a new home in California. One of the perks of the promotion was that Salazar's employer promised to pay a discount point on the purchase money mortgage for the new residence. The following statements are all incorrect EXCEPT
  - A. a discount point decreases the upfront yield of the loan originator.
  - B. one discount point will be one percent of the purchase money mortgage.
  - C. discount points can only be paid by the borrower of the purchase money mortgage.
  - D. paying a discount point is especially advantageous for a mortgagor if the loan is refinanced.
2. Elizabeth Bartell, a lifelong high school teacher and the widow of an Air Force pilot, purchased a single-family residence in California, and received a deed from the seller when title transferred. Bartell got a purchase money mortgage from a major institutional lender. She did not make a down payment and was not required to purchase any insurance to protect the lender from risk in the event of a future default. What type of financing did Bartell most likely get?
  - A. The VA home loan
  - B. The FHA home loan
  - C. The CalVet home loan
  - D. A conventional home loan
3. An owner of a parcel of real estate took out a loan, pledging the realty as security for the loan. Who signed the deed of trust?
  - A. Mortgagor
  - B. Mortgagee
  - C. Beneficiary
  - D. Holder of a nonfreehold estate

## LAWS OF AGENCY AND FIDUCIARY DUTIES

### True/False Questions

1. The principal may or may not be the person who pays the agent their commission.
  - A. True
  - B. False
2. The brokerage firm owns all the contracts of its salespeople.
  - A. True
  - B. False
3. Agency agreements must be in writing.
  - A. True
  - B. False
4. Agency by ratification is created when a previously unauthorized action is confirmed by a principal.
  - A. True
  - B. False
5. An agent owes a principal fiduciary obligations.
  - A. True
  - B. False
6. The agent's role in a transaction is to consider their own interests first.
  - A. True
  - B. False
7. An agent may not make a secret profit from an agency relationship.
  - A. True
  - B. False
8. Agency must be disclosed at any time before closing the transaction.
  - A. True
  - B. False
9. Undisclosed dual agency is not illegal.
  - A. True
  - B. False
10. Salespersons may not represent themselves as buyer or seller in a transaction.
  - A. True
  - B. False
11. If a licensee is representing a relative as a principal, this must be disclosed to the third party.
  - A. True
  - B. False
12. Death of the salesperson will terminate an agency relationship.
  - A. True
  - B. False
13. Both principal and agent must agree to the termination of an agency.
  - A. True
  - B. False
14. In a real estate listing agreement, the commission is earned when the escrow closes.
  - A. True
  - B. False
15. The agent must be the procuring cause to be entitled to the agreed-on compensation.
  - A. True
  - B. False
16. The agent only owes a duty of full disclosure of material facts to their principal.
  - A. True
  - B. False
17. An agent need not reveal that an occupant of the property was afflicted with or died from AIDS.
  - A. True
  - B. False

### Multiple-Choice Questions

1. A broker rented out an unused office room in the small brokerage firm. The tenant did not work in real estate. One day, a client came to the brokerage firm to give \$5,000 cash to the broker. The only person in the brokerage firm at that time was the tenant. The client, believing the tenant was an employee of the broker, gave the tenant \$5,000 in cash. The tenant stole the \$5,000 and disappeared. If the broker is prevented from testifying that there was no agency relationship between the tenant and the broker, it is MOST likely due to the following
  - A. ostensible agency.
  - B. agency by estoppel.
  - C. agency by conversion prevention.
  - D. agency by estoppel and ostensible agency.

2. Brian Lee is a very successful broker who solely owns and runs an independent brokerage company. Lee refuses to work outside of the county in which he was raised and still currently lives. The broker tells prospective sellers that, while commissions are generally negotiable, he will not accept a listing for less than a 7% commission, and preprints the 7% commission rate into his listing agreements. Lee also informs his prospective clients that the listing agreement must be the exclusive right-to-sell. Which of these activities is in violation federal antitrust laws?
  - A. Restricting the geographic area to one particular county
  - B. Refusing to accept less than a 7% commission rate
  - C. Refusing to accept anything other than an exclusive right-to-sell listing agreement
  - D. Preprinting the 7% commission rate in the listing agreement
3. A listing agent hired a newly licensed salesperson. The salesperson brought a listing into the brokerage firm. During a discussion with the seller, the salesperson learned that the seller had recently lost several large lawsuits and that the seller's credit score had been damaged by delinquent credit card debt. The salesperson told this to a prospective buyer who was unrepresented by a real estate agent. Providing this information to the prospective buyer was
  - A. a breach of the listing agent's fiduciary duty of confidentiality.
  - B. acceptable because the salesperson was not an agent to the seller.
  - C. acceptable because a full disclosure of material facts is owed to nonclient third parties.
  - D. fulfilling the listing agent's fiduciary duty of disclosure to the buyer.

## PRACTICE OF REAL ESTATE AND DISCLOSURES (INCLUDES SPECIALTY AREAS)

### True/False Questions

1. As an exception to commingling, the broker can place up to \$200 of his own money in a trust account.
  - A. True
  - B. False
2. The purpose of trust fund management is to commingle a broker's funds with trust funds.
  - A. True
  - B. False
3. Steering is the act of directing people of different races, religions, national origins, et cetera to or away from particular areas as a means of discrimination.
  - A. True
  - B. False
4. Redlining is the prohibited act of refusing to loan in certain areas.
  - A. True
  - B. False
5. When advertising a property, a licensee must disclose that the property is offered through a licensed real estate agent.
  - A. True
  - B. False
6. An advertisement of a mobile home for sale must be withdrawn within three days after receipt of notice that the mobile home is no longer available for sale.
  - A. True
  - B. False
7. Brokers are responsible for maintaining adequate and accurate trust fund records for three years.
  - A. True
  - B. False
8. Brokers are only responsible for supervising licensees who are employees but not independent contractors.
  - A. True
  - B. False
9. Unlicensed sales assistants may not prepare a comparative market analysis.
  - A. True
  - B. False
10. The real estate commissioner is appointed by the governor of California.
  - A. True
  - B. False
11. Real estate brokers and salespersons must complete 45 hours of DRE-approved continuing education every four years.
  - A. True
  - B. False
12. The education requirements for a real estate broker's license is eight college-level courses.
  - A. True
  - B. False
13. The amount paid out from the Recovery Fund is limited to \$50,000 per transaction.
  - A. True
  - B. False
14. If a recovery is allowed against a licensee, the real estate license of that person is automatically revoked.
  - A. True
  - B. False
15. The REALTOR® Code of Ethics is based on the Golden Rule.
  - A. True
  - B. False
16. The e-Pro certification is the National Association of REALTORS® training program to certify real estate professionals as internet professionals.
  - A. True
  - B. False
17. A resident property manager must have a real estate licensee.
  - A. True
  - B. False
18. In a gross lease, the tenant pays for all property expenses.
  - A. True
  - B. False

19. There is a seven-day right to rescind an offer to purchase a time-share.
  - A. True
  - B. False
20. The Real Estate Transfer Disclosure Statement (TDS) details the mechanical and structural conditions of the property in a form specified by law.
  - A. True
  - B. False
21. Disclosure must be made if the seller or the seller's agent has knowledge of the designation of areas of potential flooding or a list of properties, including the seller's property, has been posted at the county recorder's office, county assessor's office, and county planning agency.
  - A. True
  - B. False
22. Real estate law prohibits failing to disclose to a prospective purchaser or lessee facts that materially affect the value or desirability of the property.
  - A. True
  - B. False
23. A real estate agent is deemed responsible not only for what is known or accessible but also for what the agent should have known, following a reasonably competent and diligent inspection.
  - A. True
  - B. False
24. A disclosure known as a public report must be provided to purchasers in new subdivisions.
  - A. True
  - B. False
25. Simple multicultural etiquette can lead to success with new clients and customers.
  - A. True
  - B. False

### Multiple-Choice Questions

1. Fair housing laws prohibit discrimination against members of protected classes. Here are several protected classes: creed, gender identity, medical condition, sexual orientation, and source of income. These classes are
  - A. protected under federal, but not California, fair housing laws.
  - B. protected under both California and federal fair housing laws.
  - C. protected under California, but not federal, fair housing laws.
  - D. not protected under either California or federal fair housing laws.
2. A listing agent published a small advertisement in a promotional flyer delivered for free to a local neighborhood. Here is the entire advertisement: "4-bedroom, 3.5-bathroom, 3-car garage, single-family residence. Lot size 10,000 square feet. Beachfront property with spectacular ocean views. \$3,500,000. Great remodeling potential. Call 444-444-4444." This is
  - A. a blind advertisement in violation of both California statutory law and DRE regulations.
  - B. a blind advertisement, unless the listing agent has a real estate license with an MLO endorsement.
  - C. a blind advertisement, unless the property is subject to regulation by the California Coastal Commission.
  - D. acceptable, if buyers will be told at first point of contact that a licensee is involved in the transaction.
3. Barbara Jordanson is a real estate broker running her own large, independent brokerage firm. Jordanson, the broker of record for the firm, is busy and wants to delegate some supervisory activity to a branch or division manager. Which of the following parties will be unable to serve in this position?
  - A. A salesperson who worked full time last year in real estate
  - B. A salesperson who worked full time the last two years in real estate
  - C. A broker associate with one week at the brokerage firm
  - D. A broker associate with two weeks at the brokerage firm

4. It is illegal to engage in activities for which a real estate license is required without having an active and valid California real estate license. Which of the following parties is NOT exempt from this general licensing law?
  - A. A 102-year-old man managing his own real estate
  - B. An attorney-in-fact acting under a power of attorney
  - C. An attorney-at-law working professionally for a client
  - D. An attorney-at-law working as a commercial real estate agent
5. A listing agent was holding an open house for a newly listed single-family residence. The home had three bedrooms, two bathrooms, a three-car garage, and a view of the city. Privately, the listing agent felt the home was modest and the view of the city was unimpressive. When prospective buyers viewed the property, the listing agent said, "Look at this house! It's fantastic! This is the most beautiful view of the city in the entire subdivision!" This is MOST likely
  - A. misrepresentation and illegal.
  - B. puffing and illegal.
  - C. duress and illegal.
  - D. puffing and unethical.
6. A long-time client asks a real estate broker for assistance in buying a parcel of real estate with a manufactured home situated on it. The manufactured home was built five years ago. The client wants to finance the entire purchase not with a chattel mortgage but with a traditional mortgage secured by the real estate. Which of the following will NOT prevent the client from completing this purchase with this type of purchase money mortgage?
  - A. There is no affixture affidavit.
  - B. The manufactured home was built according to HUD building codes.
  - C. The manufactured home is still equipped to be transported on a highway.
  - D. The manufactured home is registered with the California Department of Housing and Community Development (HCD).
7. Which of the following reports is legally required for the purchase transaction of a one-to-four-unit residential dwelling?
  - A. CLTA or ALTA preliminary report of title insurance
  - B. Home inspection report
  - C. Pest control report
  - D. None of these

## PROPERTY VALUATION AND FINANCIAL ANALYSIS

### True/False Questions

1. An appraisal is the appraiser's opinion of a property's market price.
  - A. True
  - B. False
2. Market value is subjective.
  - A. True
  - B. False
3. Market price is the actual price paid in a transaction.
  - A. True
  - B. False
4. Cost is an essential element of value.
  - A. True
  - B. False
5. The four elements of value can best be remembered with the acronym DUST.
  - A. True
  - B. False
6. The three methods of estimating value can best be remembered by the three Cs.
  - A. True
  - B. False
7. The cost approach requires descriptions of comparable properties.
  - A. True
  - B. False
8. For properties that exhibit a high degree of similarity, the sales comparison approach is the most significant.
  - A. True
  - B. False
9. In the sales comparison approach, the appraiser adjusts the sales price of the subject property.
  - A. True
  - B. False
10. The most frequently used method to find the reproduction or replacement cost is the square-foot method.
  - A. True
  - B. False
11. A certified residential appraisal licensee may appraise a commercial property up to a transaction value of \$350,000.
  - A. True
  - B. False
12. The process of weighing the different values by their relevance to the appraisal problem is called reconciliation.
  - A. True
  - B. False
13. The gross income multiplier is an accurate enough method to serve as the sole means of determining market value.
  - A. True
  - B. False
14. The capitalization rate is the property owner's expected rate of return.
  - A. True
  - B. False

**Multiple-Choice Questions**

1. Two single-family residences are on opposite sides of the same street. They were built the same year, and both have the same floorplans. Both homes have three bedrooms, two bathrooms, and a three-car garage. The two residences have the same general amenities and were properly maintained. The appraiser for the home on the north side of the street appraised the property at a lower value than the property on the south side of the street. Which of the following is a likely cause for that lower estimate of value?
  - A. Two prior owners, both now deceased, never signed off on a deed.
  - B. There are more monetary liens on the property than its current market value.
  - C. Both of these.
  - D. Neither of these.
2. An appraiser was hired to appraise a historic home. The neighborhood in which the property was situated had mostly modest tract homes, some of them over 40 years old, but many renovated to reflect contemporary tastes in residential housing. The subject property had been designed and built over 50 years ago by a world-famous architect. The entire property—including the historic features—had been carefully and conscientiously preserved by the owners. Which of the following methods of appraising will be considered by the appraiser in the reconciliation process?
  - A. The market data approach
  - B. The cost approach
  - C. The income approach
  - D. All of these

## TRANSFER OF PROPERTY

### True/False Questions

1. The extended coverage title insurance policy is primarily for the benefit of lenders.
  - A. True
  - B. False
2. A quitclaim deed is the only form of deed that conveys after-acquired title.
  - A. True
  - B. False
3. A reconveyance deed will most likely be used in conveyance from grandfather to grandson in consideration of grandson's love and affection.
  - A. True
  - B. False
4. A real estate broker need not be licensed as an escrow agent to perform the duties of an escrow.
  - A. True
  - B. False
5. The fiscal year for property taxes begins on July 1.
  - A. True
  - B. False
6. The grantee is required to sign the deed.
  - A. True
  - B. False
7. A partition action is brought by a co-owner of property to force a severance of the co-owner's respective interests.
  - A. True
  - B. False
8. Right of survivorship in a joint tenancy overrides a will.
  - A. True
  - B. False

### Multiple-Choice Questions

1. Olivia Garcia, an elderly woman, owned a condominium unit. Mark O'Brien, her nephew, mistakenly thinking she had already died, sold the condo unit to Benjamin Bradford. After the conveyance to Bradford, Olivia Garcia died and left the condo unit to Mark O'Brien. Olivia Garcia died debt free. After the simple probate was completed, the condo unit was transferred to Mark O'Brien. The following statements are all incorrect EXCEPT
  - A. if the conveyancing document to Bradford was a quitclaim deed, Bradford owns the condo unit.
  - B. if the conveyancing document to Bradford was a trust deed, Bradford owns the condo unit.
  - C. if the conveyancing document to Bradford was a trustee's deed, Bradford owns the condo unit.
  - D. if the conveyancing document to Bradford was a grant deed, Bradford owns the condo unit.
2. A seller prepaid property taxes on the subject property for the current fiscal tax year. Title was transferred 1½ months before the end of the current fiscal tax year. The buyer was responsible for the day of the closing. Using the 30/360-day count convention for proration calculations, for how many days will the buyer be credited for the prepaid property taxes?
  - A. 45 days
  - B. Depends on number of days in each of the two months
  - C. Insufficient evidence given to answer the question
  - D. None

3. A borrower missed a mortgage payment. The lender properly attempted to contact the borrower, but was unable to do so. The lender then reached out to the trustee to begin the nonjudicial foreclosure process. The trustee recorded the first notice, and properly sent a certified copy to the borrower. Three months later, the trustee recorded a second notice, and sent a certified copy to the borrower. Twenty days after the second notice was recorded, the trustee held the foreclosure sale and conveyed the property to a new owner. What was the name of the first notice, the second notice, and the deed?

- A. Notice of Default, Notice of Trustee's Sale, and Deed of Reconveyance
- B. Notice of Default, Notice of Trustee's Sale, and Trustee's Deed upon Sale
- C. Respondeat Superior, Lis Pendens, and Certificate of Sale
- D. Constructive Notice, Actual Notice, and Lieu Deed

4. An owner of a parcel of real estate was in a car accident and remained in a coma for several months. Throughout her lengthy and expensive rehabilitation, she was incapable of signing anything on her own behalf. Prior to the accident, the owner was not in an agency relationship and had not executed a power of attorney (POA). During the owner's incapacity, who would have signed the deed when her real estate had to be sold to pay for her medical expenses?

- A. Her attorney-in-fact
- B. Her implied agent
- C. Her conservator
- D. The escrow officer



# ANSWER KEY

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## Unit 1

### True/False Questions

1. **B** The two classifications of all property are real property and personal property.
2. **A** The bundle of rights includes the legal rights of ownership (possession, use, enjoyment, disposition, and exclusion).
3. **A** Land includes the substances beneath the surface that extend to the center of the earth.
4. **B** A fixture is an object that was once personal property that has been attached to land as to become real property.
5. **B** Trade fixtures and emblements are exceptions to the law of fixtures and considered personal property. Therefore, they are transferred by a bill of sale.
6. **B** Real property cannot be moved.
7. **A** Mineral rights include solid minerals, such as gold, coal, and iron, as well as fluid minerals, such as oil and gas.
8. **A** The government controls the airspace and can impose building height restrictions.
9. **B** Land bordering a river is an example of riparian rights. Examples of appurtenances include easements, rights-of-way, and condominium parking spaces.
10. **A** Personal property is not attached to the land and is movable. Examples are a refrigerator, a range oven, and a washer and dryer.
11. **A** An encumbrance is any claim, right, or interest held by a party who is not the legal owner of the property—a nonpossessory interest.
12. **A** This means that there is some reason why the owner's interest is less than perfect.
13. **B** A lien is a type of encumbrance to secure payment of a debt. A deed restriction is a privately created control on land use that protects property values.
14. **A** The dominant tenement benefits from the easement, and the servient tenement is burdened by the easement.
15. **A** Ownership by an individual is ownership in severalty.
16. **B** With tenancy in common, shares can be unequal—for example, 60%/40% or 70%/30%.
17. **B** Right of survivorship means that when a cotenant dies, the survivors receive the deceased's share.
18. **A** Spouses and registered partners are equal owners regarding community property.
19. **B** A metes-and-bounds description starts and ends at a designated point called the point of beginning.
20. **B** The description follows each boundary for a given distance, in a clockwise direction and at a precise angle from the last point.
21. **A** A memory aid to remember this number is 7-11 ( $4 + 3 = 7$  and  $5 + 6 = 11$ ).
22. **A** In this system of legal description, a subdivision map filed in the county recorder's office shows the boundaries of all the parcels in the subdivision.
23. **B** These three government actions are examples of police power.
24. **A** Eminent domain is the government's right to take private land for public use.
25. **B** Property taxes are paid to the county where the property is located and are enforced by a foreclosable lien.
26. **A** Escheat is exercised when a property owner dies intestate and without heirs.

27. **B** Police power enables government bodies to exercise public control of land.

28. **A** Police power is how the government tells its citizens how they can use the land.

29. **A** Typical zoning classifications are residential, commercial, industrial, agricultural, and mixed use.

30. **B** Setback restrictions limit the location of improvements in relation to property lines. Nonconfirming use allows an owner to continue present use that no longer complies with current zoning; this is also called grandfathering.

31. **A** Since 1978, the use of lead-based paint in housing has been prohibited by the federal government. Therefore, property built before 1978 is called “target housing.”

32. **B** Radon gas, which is caused by the decay of uranium underneath the soil, is an odorless gas that enters through cracks in the basement and can cause lung cancer.

33. **B** Asbestos is a material that was used as insulation. Asbestos dust can cause respiratory disease and cancer and must be removed by a licensed professional.

34. **A** This is a report that assesses the probable impact of a proposed project on the environment.

35. **B** A covenant is an agreement to do something or to refrain from doing something. The penalty for noncompliance is typically monetary damages or an injunction.

36. **A** Deed restrictions are privately created controls on land use that protect property values and the interest of property owners.

37. **A** Covenants, conditions, and restrictions are used to establish the rules and regulations of a neighborhood.

38. **B** Deed restrictions must be for lawful purposes.

39. **B** Littoral rights are incidental to ownership of land abutting a body of water that is not flowing, such as a lake or ocean.

40. **A** Riparian rights are incidental to ownership of land abutting flowing water.

41. **B** If the stream is navigable, the state owns the land under the stream and the riparian landowner’s property line is the mean high water line of the stream.

42. **A** They may withdraw only that water for which they have a beneficial use on their property.

43. **A** Condominium owners have fee simple ownership in their unit plus an undivided interest in common elements as tenants in common transferred by a deed.

44. **A** Because there is no ownership of the unit, the owner does not receive a deed.

45. **B** A buyer of a time-share has a seven-day right of rescission.

46. **A** A planned unit development consists of separately owned parcels of land together with membership in an association that owns the common areas.

### Multiple-Choice Questions

- D** The R-3 designation generally means residential property with more than one unit (e.g., a duplex is zoned R-3).
- A** The Civil Code defines this form of ownership as a condominium.
- A** Condominiums are able to utilize a smaller space for more units and, therefore, will undoubtedly become more popular due to the increase in land values.
- C** Percolation tests are used to determine the ground’s ability to pass fluids through the soil and remove impurities.
- D** A plot plan shows the layout of improvements on a property site (a plot). The plot plan usually includes location, dimensions, parking areas, landscaping, and the like.
- A** A hip roof has four sloping sides.

7. **D** Backfill is used in construction to replace excavated earth into a hole or against a structure.

8. **B** An elevation is a side, front, or rear view of a structure.

9. **A** Real property consists of that which is immovable by law.

10. **D** When personal property (movable) becomes affixed to land, it becomes real property (for example, fence posts when installed). Personal property may be conveyed (alienated) using a bill of sale or hypothecated (pledged) as security for a loan.

11. **C** All property is either real property or personal property.

12. **A** Time of annexation is not a test of whether an item is a fixture of real property or whether it is personal property. The acronym MARIA lists which tests are the criteria:  
Method of attachment  
Adaptability  
Relationship between the parties  
Intention of the parties  
Agreement of the parties

13. **B** As between buyer and seller, strict interpretation of “real property” is given if there is no specific agreement otherwise. Until the corn is sold, harvested, or mortgaged, it is real property on the land of a seller who cultivated it. (On leased land, the lessee has the right to the crop.) Growing crops are part of the second category of real property: things attached to land.

14. **A** Of the four choices given in this question, only a stud in the wall of a house is real property. A stud is a vertical framing member of a wall to which horizontal boards are attached. They are the supporting elements in walls or partitions.

15. **D** All three notices—Notice of Nonresponsibility, Notice of Completion, and Notice of Cessation of Labor—have important effects on the time of filing and the validity of a mechanic’s lien.

16. **C** A blanket encumbrance is one that burdens more than one piece of land. This is possible with a mortgage, trust deed, or mechanic’s lien. Tax liens, however, are levied against only individual parcels of land and therefore cannot be blanket encumbrances.

17. **C** An easement is the right to use another’s property without payment. Although it is an interest in real property, it is not an estate.

18. **A** Of the choices listed, only a license is not a money claim or lien. It is a revocable right to use property.

19. **D** Judgment liens are issued by a court without permission of the owner. They create a claim on any property owned or acquired by the judgment debtor in the county in which they are recorded.

20. **C** Time in which to file mechanic’s lien:  
90 days if NO Notice of Completion: Everyone  
60 days if YES Notice of Completion: Prime contractors  
30 days if YES Notice of Completion—All others  
Time in which to start foreclosure: 90 days from recording of lien

21. **C** The period in which a mechanic’s lien may be filed will vary from 30 to 90 days. Depending on the circumstances, the lender will not release the final payment until the lien period has expired.

22. **D** A beneficiary of a trust deed has a lien on the real property, and the lien is a security interest in all of the land, fixtures, and appurtenances thereto. No changes of any kind that will change that real property or the priority of the lien can be made without the consent of the holder of the security interest.

23. **B** Under a mortgage and a trust deed, the security for the loan is the property. A mortgage has two parties; a trust deed has three. A mortgage promises the title; a trust deed conveys the legal title from trustor to trustee. The power-of-sale clause in a trust deed never outlaws under the statute of limitations.

24. **D** All three of the choices given “run with the land.” Covenants are encumbrances that remain on the land when the property is transferred. Stock in a mutual water company and appurtenant easements name real property rights that are transferred with the land when property is transferred.

25. **A** \$30,000 net from foreclosure  
- 6,000 due materialmen and mechanics\*  
\$24,000 balance to lender  
\*Because material was delivered prior to recording of the deed, all lien claimants have priority over the trust deed.

26. **A** Davidson has a personal right to use Perkins's property (servient tenement). Because Davidson does not own property, and therefore there is no dominant tenement, it is an easement in gross.

27. **B** An encumbrance is anything that affects or limits the fee simple title to real property.

28. **A** A lien makes specific property security for the debt.

29. **B** An easement is the right to use another's property without payment. Although it is an interest in real property, it is not a “possessory” interest and therefore is not an estate.

30. **D** The terms *ingress* and *egress* refer to the right of the easement holder to cross over the property of another to enter or exit from his property: an easement.

31. **D** Easements pass automatically upon transfer of the dominant tenement. The first statement is incorrect, because the dominant tenement is benefited, not burdened, by the easement. The second statement is incorrect, because an easement can include, besides rights-of-way, the right of receiving air, light, or heat; the right of using a wall as a party wall; or the right of flooding land, among other things. The third statement is incorrect, because an easement is an encumbrance but not a lien.

32. **C** While, in fact, the lessor (landlord) has a freehold estate on the property, she has given a tenant the right to possess the property for a period of time using an instrument called a lease. This lease is a piece of paper, and it is the personal property of the landlord (lessor).

33. **A** In any co-ownership, including tenancy in common, there is the unity of possession.

34. **D** *Tenancy* is the mode of holding ownership interests. The estate may be held in joint tenancy, tenancy in common, or less-than-freehold tenancy, such as an estate for years.

35. **D** A tenancy for a specific term (estate for years) ends at the expiration of the term without notice. A tenancy at sufferance is not entitled to a notice. At common law, an estate at will was terminated without notice. California statutory law requires notice to terminate an estate at will.

36. **B** *Alienate* means to transfer the title to real property from one person to another. Involuntarily alienation could occur by the operation of law, as in the case of foreclosure due to nonpayment of taxes or other lawful debts.

37. **C** *Lis pendens* (suit pending) is a notice filed or recorded for the purpose of warning all persons that the title or right to the possession of certain real property is in litigation. It is recorded to give constructive notice of pending litigation.

38. **B** The owner who sells her interest is conveying the fee title (a freehold estate) to the buyer. When the seller becomes a lessee of the former property through a leaseback arrangement, the seller has converted the former freehold (fee) estate to a less-than-freehold estate (a lease).

39. **A** Tenancy is a method or mode of holding title.

40. **D** Undivided interest means that owners cannot locate their particular interests in a property. All owners have access to every portion of the property. For example, an owner with a 10% share owns 10% of every inch of the property, not an identifiable 10% section of the property. The incorrect answer choices relate to tenants in common. Tenants in common may or may not have equal shares, and they are not required to take title at the same time. Equal shares and a unity of title are requirements of a joint tenancy.

41. **B** Fee simple estate is the greatest interest that one can have in real property. It is an estate that is unqualified, of indefinite duration, freely transferable, and inheritable. However, a fee estate can be encumbered.

42. **C** Joint tenancy's most distinguishing characteristic is its right of survivorship. Upon the death of a co-owner, interest of the deceased is dissolved and goes to the co-owner(s) without probate. Joint tenancy requires the four unities of time, title, interest, and possession.

43. **D** A tenancy in common is created when two or more persons own undivided interests in a property without the right of survivorship. If an owner dies, the deceased owner's interests go to the heirs/devisees.

44. **A** Fee simple absolute estate: Both estate of inheritance and greatest interest held in land apply; however, greatest interest held in land best describes the absolute estate.

45. **D** Civil Code section 683 enables joint tenancies to be created by (1) simple will or transfer, (2) transfer from sole owner to himself or herself and others, (3) transfer from tenants in common or joint tenants to themselves or to themselves and others, (4) transfer from husband and wife (holding title as community property or otherwise) to themselves or to themselves and others, and (5) transfer to executors of an estate or trust.

46. **C** Two sections equals 2 sq. mi.  
10% of a township = 0.10  
 $(1/10) \times 36 \text{ sq. mi.} = 3.6 \text{ sq. mi.}$   
 $5,280 \text{ ft.} \times 10,560 \text{ ft. (2 miles)} = 2 \text{ sq. mi.}$

47. **D** A commercial acre is the remainder of an acre of newly subdivided land after the deduction of areas devoted to streets, sidewalks, curbs, and the like.

48. **C** The passage is an example of a metes-and-bounds description of land. (Metes are measurements of length, and bounds are measurements of both natural and artificial boundaries.)

49. **D** The land description in a survey should contain all three items listed in the answer choices.

50. **C** The fiscal year commences on the first day of July and ends with the 30th of June following.

51. **A** The primary function of the county assessor is to establish an assessment roll each year that reflects the assessed value of real property within the county.

52. **A** A zoning authority changing use is an exercise of police power, not eminent domain.

53. **B** Zoning by cities and municipalities is a good example of the exercise of police power. The taking of private property for use by a municipality and condemnation of property by the federal government are closely related to acts under eminent domain. Restrictions in a deed are private restrictions.

54. **C** The four public limitations to private ownership of real estate are police power, eminent domain, taxation, and escheat. The establishment of rent control, land-use planning and zoning, and building ordinances and permits are all exercises of police power. Taxation and police power are two different government rights in land.

55. **C** Zoning by cities and municipalities is a good example of police power. The taking of private property for use by a municipality and condemnation of property by the federal government are closely related to acts under eminent domain. Restrictions in a deed are private restrictions.

56. **B** All zoning laws and ordinances are based on the premise that they will promote the general health, safety, and welfare of the citizens under police power.

57. **B** California sales tax applies to most tangible personal property. The tax is based on the sales price and not on the value of the goods.

58. **D** Spot zoning, a conditional use permit, and a variance are all remedies to the described situation. All allow a change in the local zoning ordinances, which permits a particular use not consistent with the area's zoning classification. Such remedies may be granted from the local zoning board of appeals for a small area provided that (1) undue hardship can be shown, and (2) the use permitted is still consistent with the general plan of the area.

59. **A** The second installment becomes due on February 1 and becomes delinquent on April 10.

60. **A** Annually, the tax collector publishes a notice of sale of real property for which taxes are delinquent. This is not a sale but a declaration of default denoting the beginning of a five-year redemption period. This declaration of default must be made on or before June 30, usually the last business day of the month.

61. **C** In most cases, laws (including zoning ordinances) that are retroactive cannot be enacted. In ridding an area of nonconforming uses of the land, the courts and zoning authorities, in order to satisfy the policy of gradual and eventual elimination of such nonconforming uses, employ the methods of prohibition of rebuilding, prohibition of expansion, and allowing a reasonable time (amortization period) within which the abuses may be eliminated.

62. **B** Public utility companies and similar public and semipublic bodies may exercise the power of eminent domain.

63. **C** This change in zoning would cause the existing apartment building to become a nonconforming use. The structure may be maintained, but enlarging or rebuilding is generally disallowed.

64. **D** Escheat is the reverting of property to the state when a person dies intestate (without a will) and the individual has no heirs to receive the property through intestate succession.

65. **A** Assessment liens and real estate taxes will take priority over any other type of lien. This is true even though the assessment liens may be created subsequent to a recorded lien.

66. **D** The two state laws that regulate subdivisions are (1) the California Subdivision Law (Subdivided Lands Law) and (2) the California Subdivision Map Act. The Map Act requires the local governing authorities (usually delegated to the planning commission) to standardize regulations regarding the physical aspects of the subdivision.

67. **A** The law specifies that on-sale general licenses may not be issued to a bona fide club in existence for not less than one year. This applies to such clubs as fraternal organizations as well as golf, swimming, yacht, and tennis clubs.

68. **C** The purpose of the Franchise Investment Law is to protect the prospective franchisee before purchasing the franchise, by requiring the franchisor to give a full disclosure statement at least 48 hours prior to the effect of a binding contract and to protect from fraud or unfulfilled promises.

69. **B** A conversion of an apartment building into five or more condominium units is a subdivision under both the Subdivision Map Act and the Subdivided Lands Act.

70. **C** The Government Code of the State of California enables the legislative body of a city to “regulate the construction, repair, or alteration of buildings pursuant to Health and Safety Code § 15153.” Although the city may also “establish building materials that might be used. . . .”, they cannot dictate . . . “the cost of the materials used.” The size and height are functions of zoning (land use), not local building codes.

71. **A** The lien and attachment laws are created by the legislative bodies of the state. A state-enabling act gives legislative powers to local governing authorities, such as city councils and county boards of supervisors, to enact local ordinances.

72. **C** Actual knowledge of lead-based paint used on a one-to-four-unit residential dwelling must be disclosed, even if construction began after January 1, 1978. The prospective buyer’s plans to demolish the structure and rebuild does not alter the disclosure requirements. Target housing is residential dwellings of one to four units constructed before January 1, 1978, but actual knowledge must be disclosed, even if construction started after that date.

73. **B** Radon gas is considered an environmental hazard. Environmental hazards result from human intervention, usually through methods or construction or installation. Old methods of construction allowed radon gas to move through the improvements and up into the atmosphere. Modern methods of construction trap radon gas in buildings, resulting in the need to mitigate the environmental hazard. Mitigation is accomplished through ventilation systems that vent the gas out of the building. A percolation test is unrelated to radon gas: A percolation test is completed to determine the water absorption rate of soil, particularly in contemplation of new construction.

74. **A** Restrictions imposed by deeds may restrict, for any legitimate purposes, the use or occupancy of land. Restrictions that are unlawful, impossible of performance, or in restraint of alienation are void.

75. **D** A condition precedent does not run with the land, is not a servitude (land burden), and, being a condition, is not a covenant. A condition subsequent runs with the land. An easement is a servitude upon the land.

76. **C** A license is a personal, revocable, and unassignable permission given to another, as distinguished from an easement.

77. **B** Deed restrictions, as a rule, are initiated for the protection of property owners. They are reasonable limitations on ownership to safeguard property values. An owner is very unlikely to place restrictions on a property that would make the property unmarketable. Zoning is a legally imposed restriction on the use of the site. A site’s highest and best use may not necessarily be any of the uses designated by a zoning ordinance, thereby causing the property to be more unmarketable than in the case of private deed restrictions.

78. **D** Riparian rights refer to “the reasonable use of flowing water.” Some examples are rivers, streams, or other “watercourses” (water flowing through a fixed or defined channel).

79. **D** Appropriation of water flowing on the public domain consists of the capture, impounding, or diversion of it from its natural course or channel and its application to some beneficial use to the appropriator.

80. **B** The Department of Real Estate administers laws related to the sale of time-shares. Per a DRE rule, the Schmidts can get a full refund and be relieved of any further financial or legal obligations under the purchase agreement, if they request the refund within seven calendar days (seven days, not seven months). The DRE rule that time-share purchasers can rescind the purchase contract within seven calendar days is not dependent either on where the time-share presentation is given or where the time-share development is located. Parties are typically held to the terms of a binding contract, but the seven-calendar day right of rescission for time-share purchases is an exception to this rule.

81. **C** A buyer of a condominium unit buys fee title to the airspace within the condo unit. Williams does own something by herself, specifically, the airspace within her condo unit. Everything else is owned, along with the other condo unit owners as “tenants in common.” These other elements (swimming pools, tennis courts, parking structures, storage units, hallways, elevators, etc.) are called common elements. The assigned parking spaces, the balcony, the assigned storage unit are limited common elements, meaning their use is assigned to one condo unit owner—in this case, Latoya Williams.

## Unit 2

### True/False Questions

1. **A** It is a voluntary and binding agreement between two or more parties to do or not to do a specific thing.
2. **B** A valid contract contains all four legal requirements. Consent, capacity, consideration, and a lawful objective.
3. **A** The party who defaults in completing the contract terms will be liable to the other party for breach of contract.
4. **B** An executory contract is a contract when one or both parties need to complete part of the contract and the contract is yet to be fully performed.
5. **B** In a bilateral contract, a promise is exchanged for a promise and both parties are obligated to perform.
6. **A** An open listing, also called a nonexclusive listing, provides for a commission to the broker if the broker is the procuring cause of a sale.
7. **A** The listing broker thus has the protection of getting at least a share of the commission if another broker finds the buyer.
8. **A** This type of listing offers the brokerage firm maximum protection and the broker will give maximum effort.
9. **B** In a net listing, the broker’s compensation is whatever amount the property sells for over a previously agreed net amount. Because such an arrangement is both inherently risky and inherently suspect, it should be avoided.
10. **B** In a buyer-broker agreement, the buyer is the principal and the broker is the agent.
11. **B** It can also be an exclusive agency agreement.
12. **B** The agreement has a provision for compensating the broker in the event that the buyer enters into an agreement to purchase property that the broker introduced to the buyer.
13. **A** This is a contractual clause in the buyer-broker agreement.
14. **A** This is an important clause explaining to the buyer the broker’s possible representation of other buyers seeking similar properties.
15. **B** It is a bilateral agreement. The buyer promises to buy, and the seller promises to sell.
16. **A** Consent is reached with the following three steps: offer, acceptance, and communication of acceptance.
17. **A** The contract is executed when duties have been completed by both parties.
18. **A** The contingent purchase provision may be used when the buyer owns other property that must be sold before the buyer can complete the transaction.
19. **B** Only certain contracts must be in writing. All real estate contracts must be in writing except for leases of 12 months or less.
20. **A** An action based on a written contract must be brought within four years.
21. **B** An addendum is additional material attached to and made part of the initial agreement document. An amendment is used to make changes to a contract.
22. **B** A unilateral agreement, which is a promise exchanged for performance, is binding when the act is performed.

23. **A** Both spouses must sign the deed that transfers title to the buyer.

24. **B** Real estate loans are made using two instruments, the promissory note and the security instrument.

25. **B** The promissory note is the borrower's promise to pay. The security instrument identifies the real estate that serves as collateral.

26. **A** It establishes the underlying obligation of the loan transaction.

27. **B** The security agreement creates a lien on the property.

28. **B** It is a unilateral agreement. A potential buyer purchases the right to buy in the future from a seller who agrees to sell within a set period for a set price.

29. **A** The lease option can be a way to ensure a subsequent purchase, particularly if part of each lease payment is applied to the eventual down payment.

30. **A** It gives the owner more flexibility than an option because there is typically no set price and the seller can sell to others if the first right is not exercised.

31. **A** It converts equity into working capital without giving up possession.

32. **B** The landlord is the lessor and the tenant is the lessee.

33. **A** No examination is needed for a two-year PRLS license.

34. **A** This is true according to the Business and Professions Code.

35. **A** The contract describes the services to be provided and the prospective tenant's needs.

36. **B** The requirement is three rental properties provided within five days.

## Multiple-Choice Questions

1. **B** An executory contract is one that is to be performed, as distinct from an executed contract, which has been fully performed.

2. **C** When applied to contracts, the word *executed* means fully performed by both parties. (When the word *executed* is used in discussing deeds, it means signed.)

3. **A** A fire insurance policy can be canceled only after written notice has been given to the insured with a reasonable time for cancellation to take effect.

4. **B** A tenant in common may lease his interest without consent of the cotenants, and the lessee would have an equal right of possession of the entire farm with the other cotenants. A tenant in common who receives rent from a third party must divide such profits with the other tenants in common.

5. **C** It is essential to the existence of a contract that there be consideration. In an action for specific performance, remedy is denied unless *adequate* consideration is proved. *Good* consideration can be love and affection, whereas valuable consideration has money value.

6. **C** When there are actions still to be performed, a contract is executory.

7. **C** Because a lease is a contract that conveys possession and use, it must, in addition to *describing* the property, indicate the *term* of the possession. Furthermore, all contracts require consideration. Although the words "let and demise" are commonly used in leases, they are not required. If a tenant takes possession and pays the rent, a signature is not required because these acts imply acceptance.

8. **C** A document transferring a right or interest in real property must be signed and acknowledged by the transferor if it is to be recorded.

9. **A** The word *novation* comes from the Latin word meaning to make new.

10. **B** When the mutual consent to a contract is induced by fraud, duress, menace, or undue influence, the contract is voidable at the option of the wronged party.

11. **D** The statute of frauds requires that certain contracts be in writing to be enforceable in court; contracts that cannot be performed within one year as well as most contracts dealing with real property are included in this statute. Because the first three choices concern themselves with business opportunities, which are personal property, these transactions fall outside the writing requirements of the statute.

12. **C** Rescind means to annul the contract and restore the parties to the same position they held before they entered into the contract.

13. **D** *Laches* means delay or negligence in asserting one's legal rights. Such a delay can make a contract unenforceable.

14. **B** A rider is an addition or amendment to the original contract.

15. **D** *Voidable* indicates that the contract is binding on both parties until some action is taken by the wronged party to unilaterally rescind the contract.

16. **B** Broker Wilson acted incorrectly because an agent should present all offers.

17. **A** If the owner reserves the right to sell the property, an exclusive agency listing has been signed. This means that if any other person sells the property, the listing broker is entitled to a commission.

18. **C** In exchange for the seller's promise to pay a commission, the broker promises to use diligence. This mutual exchange of promises makes it a bilateral contract. A unilateral contract requires a promise from only one party and performance from the other.

19. **C** The other three choices all describe exclusive listing agreements, which must have a final and definite termination date, unlike open listings.

20. **D** An exchange of promises creates a bilateral contract. Because a listing is for a period of time, the contract is executory during the listing term.

21. **B** The broker does not have the authority to bind the principal to an offer. However, the broker may "obtain an offer" in order to "present it to the principal" for acceptance or rejection.

22. **D** Commissions are not set by law but by agreement of the parties. (Some exceptions are these: Article 7, Broker's Loan Law, which sets certain maximum commission rates; and probate sales commissions, which must be approved by the courts.) The usury law does not apply to commissions.

23. **C** The buyer's broker would most likely sue the "seller's broker," traditionally called the "listing agent." Brokers "cooperate" with each other to sell the properties listed on the MLS. Part of the listing on the MLS includes the compensation that the seller's broker offers to the buyer's broker for bringing a buyer to the purchase transaction. It's typically a 50-50 split, but not always. The other answer choices are incorrect. The "selling agent" is the traditional name for the "buyer's agent," so-called because the buyer's agent brings a buyer to the transaction and sells the property. Here, the selling agent is Javier Salazar, and he would be the plaintiff in the lawsuit for the unpaid commission: He would not sue himself. Because the property was listed on the MLS, the buyer's agent would not sue the seller. This might have been the correct answer many years ago, but cooperation between brokers on the MLS means it is much more likely for a buyer's agent to sue a seller's agent for an unpaid commission. Finally, without a written buyer-broker representation agreement specifying that the buyer is ultimately responsible for Javier Salazar's commission, it's not likely that he would be allowed to sue the buyer in court.

24. **B** The buyer's obligation to pay the commission set forth in the exclusive right-to-buy buyer-broker representation agreement will be extinguished if the buyer's broker accepts a commission from either the seller or the seller's agent. Otherwise, if a property is found during the term of the agreement, the buyer must pay the agreed-upon commission, even if the buyer finds the property. The exclusive right-to-buy agreement is rarely used in California, but not illegal. This is sometimes called the "exclusive right-to-represent."

25. **D** Because the liquidated damages clause of the form was not initialed, the seller may proceed against the buyer upon any claim or remedy that he may have in law or equity. This would include damages or specific performance.

26. **C** Only the seller has the right to allow the buyer to do anything with the property before close of escrow.

27. **D** The Civil Code states that any total restriction on placing a sign is void as "an unreasonable restraint upon the power of alienation."

28. **D** Because the buyer signs the offer, it should be the buyer who signs the promise (agreement) to make this earnest money deposit.

29. **A** An understanding of the terms *revoke* and *reject* is essential in these answers. An offeror revokes an offer, but an offeree can accept or reject an offer.

30. **C** An optionee acquires a contractual right but acquires no legal interest in the property until after the optionee exercises the option.

31. **D** The broker is not a party to the contract and therefore cannot sue for specific performance.

32. **D** A bilateral agreement is one in which promises are exchanged. An executory contract is related to performance and something remaining to be done by one or both parties. The agreement between broker and a salesperson is an example of a bilateral executory contract.

33. **D** A promissory note is the evidence of the debt and is secured by a deed of trust. The promissory note is not recorded, but the deed of trust is. A notice of completion and a trustee's deed must be recorded. Conditional sales contracts (also called real property sales contracts, installment contracts, or land contracts) are often recorded.

34. **A** The essence of an option is that an optionor (seller) grants to an optionee (prospective buyer) an option to purchase (or to renew a lease, etc.) a certain property under certain terms for a specified time. The option must be supported by its actual consideration, separate and independent of the purchase price of the property.

35. **C** An optionee acquires a contractual right but acquires no legal interest in the property until after exercising the option.

36. **D** In 2009, it became illegal in California for anyone to collect a fee in advance of performing work related to loan modifications or loan forbearances. A loan modification is a voluntary agreement between a lender and a borrower to modify a loan (e.g., number of payments, term of the loan, etc.). Loan forbearance is the reduction or suspension of loan payments, typically until a later date. Usually, a lender agrees to a loan modification or a loan forbearance in order to prevent a foreclosure.

## Unit 3

### True/False Questions

1. **A** In California, we use trust deed rather than mortgages as the security agreement.
2. **A** The trustor (borrower) gives legal title to the trustee (neutral third party), and the lender becomes the beneficiary.
3. **B** The deed of trust and the mortgage are the security agreements. The promissory note serves as evidence of the debt.
4. **A** It's an unconditional promise of payment negotiable in the secondary market.

5. **A** The entire principal is paid back in one lump sum at the end of the term.

6. **A** An example would be a furnished condominium.

7. **B** More than one parcel is pledged as collateral. This type of financing is typically used by builders or developers.

8. **B** Commercial banks prefer short-term loans for commercial, business, and new construction.

9. **B** Mortgage brokers act as intermediaries between borrowers and lenders.

10. **B** Mortgage bankers lend their own money.

11. **A** The life insurance company receives interest plus an equity position in income-producing properties.

12. **A** In FHA loans, the funds come from qualified lenders. Borrowers are able to purchase with a lower down payment. Property must be owner occupied.

13. **A** VA loans offer no insurance premium and no down payment.

14. **B** The California Department of Veterans Affairs administers the program and is a direct lender.

15. **A** The promissory note is a negotiable instrument that cannot be recorded.

16. **A** Covenants include default on payment, default on taxes, no adequate insurance, committing waste, illegal use, alienation without consent, and removing improvements.

17. **B** A deed of trust is a three-party instrument. The borrower is the trustor, the lender is the beneficiary, and a neutral third party is the trustee.

18. **B** A satisfaction is used to release the lien in a mortgage. A deed or reconveyance is used with a trust deed note.

19. **A** Regulation Z applies only to loans from institutional lenders to consumers for personal, family, or household purposes. It does not apply to business loans.

20. **B** APR only includes costs paid to the lender.

21. **A** RESPA prohibits kickbacks for unearned fees, such as lenders, insurance agents, escrow companies, paying money for referrals by brokers.

22. **A** One point equals one percent of the loan amount.

23. **A** This disclosure is required for all loans negotiated by licensees for one-to-four-family residential transactions.

24. **B** A broker can loan his own funds if the borrower is informed of the source of funds.

25. **B** The maximum commission depends on the loan amount, the length of the loan term, and whether the loan is secured by a first or second deed of trust.

26. **A** A finance lender is someone who is in the business of making consumer or commercial loans in which personal property may be used as collateral.

27. **A** Three types of MLOs can operate in California: mortgage loan brokers, California finance lenders, and residential mortgage lenders.

28. **B** Eight hours of continuing education annually is a requirement of MLOs.

### Multiple-Choice Questions

1. **C** The seller would be relieved of primary liability if the buyer assumed the existing loan of record.

2. **C** The effective interest rate is the percentage of interest that is actually paid by the borrower and the nominal interest rate is the percentage of interest that is stated in the loan. This statement defines correctly the effective interest rate as the percentage of interest actually paid (or received by the investor) and may reflect periodic compounding. The effective rate may also include some nonrecurring costs such as discount points and is similar to an annual percentage rate (APR) as defined by Regulation Z. The nominal rate is the percentage of interest stated in the note.

3. **B** Amortization is (1) the liquidation of a financial obligation on an installment basis or (2) recovery of cost or value over a period of time.

4. **D** Holder in due course: One who has taken a note, check, or bill of exchange in due course (1) before it was overdue, (2) in good faith and for value, and (3) without knowledge that it has been previously dishonored and without notice of any defect at the time it was negotiated.

5. **D** An anchor tenant is the key tenant in a commercial development. The developer looks for a “blue chip” firm, such as J.C. Penney or Sears. This gives the lender confidence in the expectation that the development will pay its own way.

6. **B** The basic idea of leverage is to use other people’s money to finance purchases to realize greater return on your investment. The increase is called *appreciation*.

7. **C** Liquidity is the ability to convert assets into cash at a price close to true value. Stocks that are traded publicly are a relatively liquid investment. Real estate is considered to be a longer-term investment because it is not highly liquid.

8. **D** When a lender gets his principal back in full, he suffers no direct loss, even though he may not gain as much as expected in terms of future interest not paid. Inflation can result in a lender’s being paid back with money of lower buying power. Recession and unemployment can result in borrower’s going into default with loss to a lender.

9. **C** The secondary mortgage market is the marketplace where existing loans are bought and sold by and to mortgagees. The term *mortgagee* means lender or holder/owner of the security instrument. Because there are no borrowers (mortgagors/trustors) in the secondary market, the last three answer choices can be eliminated.

10. **C** Inflation, tight money, and demand for funds are all factors that directly influence interest rates. Unemployment has the least effect among the choices presented.

11. **C** A beneficiary’s statement (a.k.a. a “bene” statement) is a statement issued by a lender giving the remaining principal balance and other information concerning the loan. Escrow agents usually write for this statement when an owner wishes to sell, assume, or refinance property.

12. **D** If market prices rise, then the property value appreciates and the borrower’s equity rises. An increased equity increases the owner’s interest in protecting the investment, making that borrower less likely to default on the loan.

13. **C** Institutional and private lenders sometimes charge a penalty fee if a conventional loan is paid off in the early years of the loan. A VA or FHA loan may be repaid in full at any time without penalty.

14. **A** The proportion of the nation’s surplus money that will enter the real estate market depends largely on conditions in the mortgage market, which may be divided into supply and demand factors. Mortgage interest rates increase when mortgage money is in short supply relative to demand for this money. Higher interest rates in nonmortgage markets attract mortgage lenders away from mortgages to other types of investments, and as a result, financial institutions have fewer funds to make mortgage loans.

15. **C** The correct choice is “causes hardship on the buyer by placing the lender of a larger sum in the favored position.” A subordination clause would not cause hardship on the buyer. The other three choices are all conditions that may result from a subordination clause.

16. **D** A default constitutes a failure to perform either (1) a duty or (2) an obligation. In order to protect their security, most deeds of trust contain agreements between the mortgagor and mortgagee, which if breached constitute a default. These agreements include the following: not to be delinquent in payments, not to use the property for other than its intended purpose, and not to fail to maintain the property. Be careful. If the question stem was phrased “The term *default* in most mortgages MOST commonly means that the mortgagor,” the correct answer would be “is delinquent in monthly payments.”

17. **C** When mortgage money is plentiful, lenders tend to drop interest rates to attract more borrowers (the law of supply and demand).

18. **A** The trustor is the owner-borrower of a property mortgaged by the use of a trust deed. As the property appreciates, the trustor’s equity increases and the trustor therefore benefits more than the other parties indicated.

19. **D** All the choices are legitimate reasons for the release schedule to be disproportionate in favor of the beneficiary.

20. **C** Mortgage bankers who assemble loans and temporarily hold these portfolios until they can be sold to investors in the secondary mortgage market are said to be warehousing loans.

21. **B** Notes that are sold for less than the face amount or less than the unpaid balance are said to be sold at a discount.

22. **B** The loan-to-value ratio is the amount of the loan as a percentage of the appraised value. Example: An \$80,000 loan on a property appraised at \$100,000 would have a loan-to-value ratio of 80%.

23. **C** The “price” of borrowed money is most commonly expressed as interest rates. These rates are set by the forces of supply and demand interacting in the open money market. The term *fluctuating money market rate* describes this “price” of borrowed money.

24. **C** In real estate finance, the term *impounds* means reserves, which is a trust-type account established by lenders for the accumulation of a borrower’s funds to meet periodic payment of taxes and insurance as they become due.

25. **C** A low loan-to-value ratio indicates a high equity. A loan-to-value ratio of \$60,000 to \$100,000 is lower than one of \$80,000 to \$100,000. In the first case, the owner has an equity of \$40,000; in the second case, the equity is only \$20,000.

26. **D** Private mortgage insurance (PMI) protection is available to lenders as additional security for low-down-payment home loans. It guarantees the lender that, should the borrower default in loan repayment, the insurer will reimburse the lender for the dollar loss suffered or on the insured amount, whichever is less.

27. **D** A lock-in clause is a clause that may appear in a note or land contract that prohibits the lende from paying off the indebtedness before the date set forth in the contract.

28. **B** A takeout loan literally takes the construction lender out of the financing picture and the construction loan is replaced with a long-term conventional loan.

29. **C** An open-end mortgage is one containing a clause that permits the mortgagor to borrow additional money after the loan has been reduced without rewriting the mortgage.

30. **A** A partially amortized loan is not fully paid off in installments. On the due date, the balance is paid off in a lump sum called a balloon payment because it substantially exceeds any individual installment. The term “amortized loan” generally means “fully amortized.” This is a loan fully paid off by installments over its term.

31. **D** A conditional/installment sales contract, commonly called a land contract, transfers equitable title to the buyer, but the seller keeps the legal title until the contract has been fulfilled.

32. **C** A hard money loan is a loan of cash, as opposed to the extension of credit by a seller.

33. **B** "Does not require conveyance of title within one year from date of formation of the contract" completes the sentence in the question. The two parts constitute a quotation from section 2985 of the Civil Code, which defines a land contract.

34. **B** When a tight money situation exists and money is difficult to get for first trust deeds and mortgages, there is an increase in secondary financing.

35. **C** The "price" of money, commonly expressed as interest rates, is determined in the market, where the principle of supply and demand is the dominant factor.

36. **A** The mortgage insurance that is available under FHA financing is for the benefit of the lender. This insurance is known as mutual mortgage insurance and is used to reimburse the lender in the event of default and deficiency.

37. **D** FHA is not a direct lender. Institutional lenders approved by FHA make loans, and the lender is insured against loss as to a certain percentage of the loan amount. The borrower pays for the insurance.

38. **D** The subdivider would go to a lender for a conditional commitment, because the buyer is yet unknown.

39. **A** On most FHA-insured mortgages, the borrower pays an up-front MIP and an annual MIP. The up-front MIP can be financed with the mortgage.

40. **C** To curb inflation, the Federal Reserve Board would raise the reserve requirements for its member banks and enter into the bond market in a selling capacity. If the Federal Reserve Board reduced reserve requirements, lowered discount rates, or bought bonds, it would make more money available and create greater inflation.

41. **B** The Federal Reserve Board could create a tight money market by restricting the flow of money and credit. It could use one or a combination of any of these three methods: (1) Raise the reserve requirement of its member banks (not in any of the choices); (2) Sell U.S. government bonds through its Federal Open Market Committee; (3) Raise the discount rate on short-term loans made to its member banks.

42. **D** When the discount rate increases, interest rates increase, making money more costly and harder to get.

43. **B** One of the features of an FHA loan is the mortgage insurance. This protects the lender against possible loss and reduces the risk to the lender.

44. **B** FHA appraisals are ordered from FHA by the lender who has agreed to make the loan, not by the buyer. This appraisal is actually a commitment by FHA to insure a loan in a certain amount if made by the ordering lender.

45. **C** The Department of Veterans Affairs is the state department that handles CalVet loans. Because the state is handling the transaction, no discount points are charged.

46. **D** The California Department of Veterans Affairs requires each borrower under the CalVet plan to apply for life and disability insurance.

47. **C** The borrower would need to know the schedule of payments for the loan. FHA loans do not have prepayment penalties. Secondary financing is not normally permitted at the origination of the first loan. Mortgage life insurance is not a requirement of an FHA-insured loan (although mutual mortgage insurance is a requirement to protect the lender against default of the borrower).

48. **A** The note is the overriding instrument and generally controls. The mortgage contract or trust deed simply gives security to the lender in addition to the promise to pay. A mortgage or deed of trust gives no additional validity to an unenforceable note.

49. **C** A three-party instrument with which real property is made security or collateral for a debt is the trust deed.

50. **D** If the buyer assumes the existing trust deed, she relieves the seller of primary liability; but the seller retains a secondary liability for any possible deficiency judgment. If the condition added “with a substitution of liability,” the seller would be relieved of all liability. If the insertion read “Take property subject to loan of record,” the words “subject to” leave the seller with the only personal liability in the event of a deficiency judgment, because a buyer who takes title “subject to” an existing loan risks only equity in the property.

51. **C** Equitable title is the right to any equity in the property. Both the vendee (buyer) and the trustor (buyer) would hold or retain equitable title.

52. **A** A “due-on-sale” clause, also called an alienation clause, is a form of an acceleration clause found in some mortgages or trust deeds authorizing the lender to call the loan when the property is conveyed. This clause eliminates the new buyer’s assuming the mortgage unless the mortgagee permits the assumption, in which case the mortgagee could increase the interest rate and/or charge an assumption fee.

53. **D** An offset statement is customarily obtained from the property owner when existing mortgages or trust deeds are assigned to an investor. It sets forth the true condition of the mortgage lien and states whether the property owner has any claims that do not appear in the instrument being purchased by the investor. The offset statement is obtained in addition to the beneficiary statement from the lender.

54. **C** A subordination clause is an agreement by the lienholder to stay in a second or a junior position with regard to the priority of subsequent loans.

55. **A** A subordination clause benefits the trustor (borrower) by making it easier for the borrower to obtain additional financing using the title of the same property as security. The lender of a prior loan that includes such a clause agrees to relinquish the priority of her trust deed to specified financing to be obtained by the borrower at a later date. Without a subordination clause, a construction lender, desiring first position, would be unwilling to finance the improvements unless the first loan was paid.

56. **B** Under RESPA, the lender must furnish a copy of a special information booklet prescribed by HUD together with a Loan Estimate of closing costs to every person from whom the lender receives a written application for a first mortgage loan. The lender must supply the Loan Estimate by delivering or placing it in the mail not later than three business days after the application is received.

57. **D** The three-day right of rescission under the Truth in Lending Act does not apply to any trust deed loan to purchase a property. It would apply to most second trust deed loans against homes when the loans are not purchase money. Loans to purchase business or commercial property or rental property are not under the Truth in Lending Act.

58. **D** The right of rescission under the federal Truth in Lending Act never applies to purchase money loans. Therefore, the Jacksons do not have a right of rescission. The Truth in Lending Act applies only to loans for personal, family, or household purposes, never to business loans regardless of what collateral is put up. Therefore, the Londons have no right of rescission.

59. **C** Kickbacks, unearned fees, and the seller designating (not the same as requesting) the title insurance company are all violations under RESPA. Buyers may, however, designate the lenders of their choice.

60. **B** RESPA requires the lender to furnish the borrower the following two items by delivering them in person or placing them in the mail not later than three business days after the application of the borrower is received: (1) a special information booklet prepared or approved by HUD that explains settlement costs; and (2) a Loan Estimate.

61. **B** An assumption fee is one of many fees that must be included in the finance charge to determine the annual percentage rate as part of a Truth-in-Lending Disclosure Statement. Among other fees not required are appraisal fees, recording and document fees, and title insurance fees.

62. **B** Federal Reserve System's Regulation Z, also known as the Truth in Lending Act, requires advertising to state the financing charge expressed as an annual percentage rate.

63. **A** Under the Truth in Lending Act, Buyer's points, time-price differential, and finder's fees must be disclosed in the finance charge. Exempted charges on residential mortgage transactions include title insurance, document costs, recording and notary fees, credit investigations, and appraisal fees.

64. **D** RESPA states that coverage is restricted to first mortgage purchase money loans secured by one-to-four-unit residential properties made by federally regulated or insured lenders.

65. **C** The federal Truth in Lending Act requires a Notice of Right to Rescind only when security for the loan is the borrower's existing principal residence.

66. **B** Provided Sanderson has a mortgage loan origination (MLO) endorsement on his real estate license, he is legally allowed to work as a mortgage loan broker, bringing together prospective borrowers and prospective lenders. Merely having a real estate license is no longer sufficient for Sanderson to work as a mortgage loan broker: Sanderson must have the MLO license endorsement. Provided all the professional and educational requirements have been met for MLO activity, it is legal for a real estate licensee to work as a mortgage loan broker and to receive compensation for mortgage broker activities.

67. **A** California statutory law, specifically Article 7 of the California Business and Professions Code, regulates the costs and commissions a loan broker can charge for regulated loans. A regulated loan is a first mortgage of *less than* \$30,000 and a second mortgage of *less than* \$20,000.

68. **B** Mortgage companies characteristically (1) participate in and supervise construction loans (and "takeout" loans); (2) solicit loans from anyone (institutional or noninstitutional lenders), represent them, and also seek out borrowers for such loans; (3) sometimes have money of their own to lend; (4) accumulate loans (warehousing) that can be sold in groups and that are readily salable in the secondary money market; and (5) service loans that are arranged by their correspondents.

69. **A** The characteristics listed describe those of an insurance company.

70. **C** Of the four listed, the Federal Savings and Loan Association is the only one operating in the primary loan market. Today, more residential loans are made by commercial banks than S&Ls.

71. **B** These are the characteristics of insurance companies.

**Unit 4****True/False Questions**

1. **A** The agent's authorized actions are binding on the principal, and the principal can be held liable if the agent's actions cause harm to a third party.
2. **A** The employing broker is responsible for all contracts, listings, and purchase agreements.
3. **B** The majority of real estate licensees are independent contractors. Some are employees.
4. **A** This is a requirement of the real estate commissioner.
5. **A** Obedience, loyalty, disclosure, confidentiality, accounting, reasonable care and skill are the fiduciary duties.
6. **B** Dual agency occurs when a broker represents more than one party to a transaction. It typically requires disclosure and written consent of both parties.
7. **B** This is the definition of a general agent. A special agent is one appointed to carry out a single act or transaction.
8. **B** The creation of an agency relationship can be made by express or implied agreement, ratification, or estoppel.
9. **B** An express agency is created by a direct statement, which may be oral or written.
10. **A** An example would be giving your neighbor advice on a real estate matter.
11. **A** Agency by ratification is established when either the principal or the agent ratifies or authorizes an activity of the other that held out an agency relationship.
12. **A** This agency is created when a third party is led to believe an agency relationship exists.
13. **B** When someone represents that another person is her agent, and a third party relies on that representation and deals with the agent accordingly, an agency by estoppel is established and the principal will not be able to evade the agency relationship.
14. **A** The agent has the obligation to use due diligence in fulfilling the purpose of the agency agreement.
15. **A** If a principal asks the agent to do something unlawful, the agent does not have to follow those directions.
16. **A** The agent's role in the transaction is to consider the interests of the principal first and foremost.
17. **A** An agent must disclose to the principal the benefits of the transaction, as well as the risks or defects.
18. **A** The agent must keep price, terms, and motivation confidential.
19. **B** Agents must account for any money or personal property entrusted to them or gained as a result of the relationship with their principal.
20. **A** The agent owes the principal the duty of reasonable care and skill in carrying out the tasks dictated by the agency agreement.
21. **B** The written disclosure must be made by the listing agent before the seller signs the listing agreement.
22. **A** The details of the agency relationship must be disclosed in writing in any transaction involving property of one-to-four residential units.
23. **A** Agents disclose and elect, and principals confirm. All three steps are done in writing.
24. **B** Disclosure is required if an agent is representing a relative.
25. **A** A standard form provided by the California Association of REALTORS® is used in our state.
26. **A** This would be accomplished with the agency confirmation form.

27. **B** A general agent has the authority to perform a series of acts for the principal.

28. **B** Only a general agent has a limited ability to bind their principal.

29. **A** An attorney-in-fact should not be confused with an attorney-at-law. Powers of attorney are normally given for specific purposes, such as to sign a deed when the owner is not available.

30. **A** Dual agency requires written disclosure and written consent of both parties.

31. **B** Undisclosed dual agency is a violation of California real estate law and Civil Code.

32. **A** Agents are allowed to represent themselves in real estate transactions as long as it is disclosed to third parties.

33. **B** Agents duties to third parties are honesty and fair dealing.

34. **B** The principal or agent always has the power to terminate the agency without the other person's consent.

35. **A** An early cancellation of a listing agreement by a seller is an example of a situation in which the seller may be liable to the listing broker for expenses or a commission.

36. **A** The third party has a right to know when an agency agreement has been terminated.

37. **B** The California Civil Code lists the ways in which an agency relationship may be terminated.

38. **B** Death of either the principal or the agent (responsible broker) would terminate an agency.

39. **A** Others are destruction of the property, agreement of the principal and agent, or by operation of law, as in a bankruptcy.

40. **B** The agent must disclose to the principal any possible conflict of interest.

41. **B** The fact that the prospective buyer is the broker's aunt must be disclosed to the seller.

42. **B** The commission is earned when the real estate broker finds a buyer who is ready, willing, and able to purchase the subject property on the seller's original terms or when the seller accepts a purchase offer at an agreed-on price and terms.

43. **B** The principal can revoke the agency agreement but may be liable for the full amount of the agent's commission.

44. **A** In an open listing, only the broker that procures the buyer will have earned a commission.

45. **A** Regardless of procuring cause, the listing broker will receive a commission.

46. **B** If the seller identifies a prospective buyer in the listing agreement as someone to whom the property may be sold without commission and that person buys the property, then no commission will be paid to the listing agent.

47. **A** A real estate agent owes a third person a duty of full disclosure of material facts.

48. **B** If the seller asks the agent not to reveal certain defects, such as termite damage, the agent must inform the principal that the agent cannot hide such information.

49. **B** "As is" means a seller will not make any repairs to the property but material defects must still be disclosed to the buyer.

50. **A** Conspicuous physical defects must be revealed, certainly, but it goes beyond that. As a rule of thumb, when in doubt, disclose.

51. **A** This case established that a broker has a duty to conduct a competent inspection of residential property and to disclose to prospective purchasers all facts revealed by the investigation that materially affect the value or desirability of the property.

52. **A** At first contact with third parties, agents must inform them to not share confidential information. Agents' fiduciary duties would require them to share that information with their principal.

## Multiple-Choice Questions

1. **C** The law requires the instrument that creates the power of attorney to be recorded when the act involves real property. The encumbering by an attorney-in-fact is permissible, provided he is not named as beneficiary.
2. **B** A minor lacks the capacity to appoint an agent under state law. A minor has the capacity to enter into contracts for necessities, but the party with whom the minor contracts runs the risk of having the minor disaffirm the contract before reaching majority.
3. **B** The broker, through the acts of the salesperson, acted in excess of authority. By accepting a check when not authorized, the salesperson created an agency between the buyer and the broker, but only with regard to the deposit.
4. **B** The attorney-in-fact is the person who holds power of attorney and is delegated to act for another.
5. **D** An agent cannot act for two principals in negotiations with each other unless both have knowledge of and consent to the dual agency. The agency could be denied commission from either, and the undisclosed dual agency is a ground for rescission by either principal. The broker's license could be revoked or suspended by the Department of Real Estate.
6. **D** The principal is liable for the acts of his agent performed "within the scope of authority." The agent is liable for the agent's own acts performed "beyond the scope of authority."
7. **B** When Katz told the prospective buyer that the owner would sell for less than the listing price, when the broker had not been specifically instructed to disclose that confidential information, the broker violated his fiduciary obligation to his principal.
8. **D** A power of attorney is a written instrument giving authority to an agent, called an attorney-in-fact. Don't confuse with attorney-at-law.
9. **D** A broker acting as an agent would not likely be able to sue her principal for specific performance because the broker is not a party to her principal's contract.
10. **C** Consideration is not required of an agency relationship. The agency may be a gratuitous agency.
11. **B** All material facts must be disclosed to all interested parties to a transaction. A material fact is one that, if known, would affect the value or desirability of the property. Frequently, material facts are negative (e.g., a leaky roof), but not always. The fact that this is a positive material fact doesn't negate the legal requirement that the listing agent disclose it to both the seller and the prospective buyer. While fiduciary duties are owed only to a principal (here, the seller), the duty to disclose material facts related to the subject property is owed by real estate licensees to all interested parties to a transaction. The other answer choices are incorrect. When the government official told the seller's agent about the mineral rights, it's as though that official was speaking directly into the seller's ear. It would be a breach of the listing agent's fiduciary duty of disclosure to assume that the seller already knows about the subsurface rights, and remain silent.
12. **D** Under the exclusive right-to-buy buyer representation agreement, the buyer's broker earns a commission if a property is found during the period of the agreement, no matter who finds the property. Typically, the seller pays the brokerage commission. But, because this seller was working without an agent, the buyer will be responsible for paying the commission the buyer and the buyer's broker agreed to during their buyer-broker contract negotiations. When a broker works "in house," that broker represents both the buyer and the seller. Here, the fact pattern tells us that the seller was working without a broker. Finally, a broker exercises "due diligence" by making a continuous, good-faith effort to perform the contractual duties owed to a principal. The fact pattern states that the buyer's broker was working conscientiously and diligently.

13. **A** If a broker sells a property through a cooperating broker and, while the transaction is in escrow, learns the cooperating broker is selling a similar property to the same buyer at a higher price, the broker must inform his principal because he has a fiduciary duty to the seller even though the transaction was in escrow.

14. **D** The written agency disclosure form must be presented to the seller before the seller signs the listing agreement. This is a requirement for both first-time and experienced sellers. An agency disclosure form must also be given to buyers, before a buyer and agent enter into a buyer representation agreement. The requirement of an agency disclosure form is not limited to single-family residences.

15. **D** For a purchase transaction, an undisclosed dual agency occurs when the broker of record at a brokerage firm serves as the agent for both the seller and the buyer without first receiving the permission of both parties in advance and in writing. The DRE disciplines real estate licensees for undisclosed dual agencies, even if they were established by accident. An undisclosed dual agency, a.k.a. a divided agency, is illegal and may very well result in the return (disgorgement) of an earned commission.

16. **D** The “selling agent” is a term that usually refers to the agent of the buyer. The buyer’s agent is called the “selling agent” because the buyer’s agent typically brings the buyer to the transaction, and is, therefore, instrumental in selling the property. The listing agent is the seller’s agent. The seller’s agent is hired when the seller signs the listing agreement. It would not be possible for a listing agent (the seller’s agent) to serve as only the selling agent (the buyer’s agent). Note: If the buyer does not have an agent, the seller’s agent might be called both the listing agent and the selling agent.

17. **D** The listing broker owes fiduciary duties to the seller. Here, one of the sellers is Joan Fortin, Ronald Brown’s aunt. Undisclosed compensation is a secret profit and the listing broker will likely be required to disgorge this secret profit to his aunt. Receiving a secret profit is also cause for discipline by the DRE.

18. **C** The listing broker had a duty to disclose that his spouse worked at, and was a part-owner of, the recommended entity. The listing broker had an indirect interest and would have profited indirectly in ABC Escrow through his spouse. Agents are allowed to recommend an entity owned by family members, but that fact should have been disclosed by the agent to the principal.

19. **B** Destruction of the improvements will terminate a listing agreement. Although land is theoretically considered to be indestructible, the improvements (the buildings) are destructible, and the destruction of the improvements will terminate the listing agreement. This rule is not dependent on whether or not a listing broker knows that a property is located in an area subject to natural hazards. A listing agreement is a contract by and between the seller and the seller’s broker. Changes to the contract must be in writing and signed by both parties. There is no automatic transformation—through operation of law—of a listing contract from one property type (a commercial office building) to another property type (vacant land).

20. **A** A listing agreement is a contract by and between the seller and the broker of record at the brokerage firm. The salesperson, Robert Wilson, is not a party to the listing agreement, and his death will not impact the listing agreement. The death of the salesperson will not automatically terminate the listing agreement or change the term of the listing agreement.

21. **C** A listing agreement establishes an agency relationship between the seller and the seller’s broker. That agency relationship terminates upon full performance of the contract. After the close of escrow, there are typically no further duties for either party to perform. The listing agent has found a buyer, and the seller has paid the listing broker’s commission. A contract in which there are no further duties or responsibilities to be completed by either party is called an “executed” contract. An “executory” contract, by contrast, is one where one or more parties to the contract still have duties to complete. An exclusive listing contract typically terminates at the close of escrow, not 6 or 12 months after the close of escrow.

22. **C** A protection clause, also called a safety clause, in a listing agreement binds the seller to the payment of a commission to the broker if the property is sold within a period of so many days after the expiration of the listing to a person with whom the broker negotiated during the listing period.

23. **D** Under Article 7, the maximum commission and fee is:  
\$4,000 2nd T.D.  $\times$  0.15  
(15% of the principal of a loan of three years or more)  
\$600 maximum commission + \$390 (5% or \$390—whichever is greater)  
\$990 maximum commission and fees

24. **C** In an exclusive right-to-sell agreement, if the owner decides to revoke the agreement, he is liable for the full commission under the listing agreement.

25. **D** Under normal circumstances, a commission is paid by check. However, as long as the principal and the broker agree, the commission may be paid in any of the forms listed.

26. **D** That an agent “gave part of his commission to the buyer” would be considered a material fact. The fiduciary relationship of the agent to the principal required full disclosure of all material facts. The agent would not be disciplined by the real estate commissioner unless the broker failed to disclose this material fact to the principal.

27. **B** The listing broker most likely engaged in “puffing.” Puffing is an exaggerated form of sales talk that a reasonable person would not rely on to make a decision. A good way to test whether a statement is puffing or not is to see if it can be measured objectively. How could you measure “the best view” objectively? It’s a subjective statement, dependent on the individual preferences of the speaker. Therefore, the broker’s comment would fall under the category of puffing. The other answers are incorrect. Misrepresentation is a lie. If the subject property didn’t have a view of the city, the listing broker’s comment would rise to the level of a misrepresentation. Perjury is lying in court after taking an oath or affirmation. There is nothing in the fact pattern to suggest that the listing broker is in court and engaging in perjury. The listing broker does not owe fiduciary duties to the buyer, unless serving as a dual agent. The test question states that the buyer was unrepresented by any real estate agent. The listing broker owes a nonclient third party honesty, fair dealing, and a full disclosure of material facts, but these are not the fiduciary duties an agent owes a principal.

28. **D** The listing agent owes nonclient third parties the duty of honesty. All these answers complied with the listing agent’s duty of honesty to a nonclient third party. If the seller states a material fact such as the floor is true mahogany wood, and the agent has no reason to suspect the seller is in error or lying, the agent is legally permitted to rely on this information when discussing the subject property with a nonclient third party. Note: This duty of honesty to a nonclient third party is not a fiduciary duty: Fiduciary duties are owed by an agent only to the agent’s principal.

29. **B** A material fact is one that affects the desirability or value of a property. Here, the racist acts in the neighborhood fall under the category of material facts that must be disclosed to the prospective buyer. The buyer's specific racial background or the fact that none of the racist acts occurred on the subject property will not alter the broker's duty to disclose. Panic peddling (a.k.a. blockbusting) is the illegal activity of a real estate licensee who induces homeowners to sell due to the prospective entry of a protected class into the neighborhood. There is nothing in the fact pattern related to panic peddling.

## Unit 5

### True/False Questions

1. **A** If a brokerage firm accepts and holds funds belonging to others, then the brokerage firm and the employing broker are required to maintain records of trust funds.
2. **B** Commingling of trust funds is mixing of trust funds with funds belonging to the agent. The actual use of trust funds for purposes other than their intended purpose is conversion and is a felony.
3. **A** And they must be open for inspection by the real estate commissioner.
4. **B** It is not a legal requirement for a broker to have a trust account.
5. **A** Although long ignored, the Act was upheld by the U.S. Supreme Court in 1968 in the case of *Jones v. Mayer*.
6. **A** It prohibits discrimination based on race, color, religion, sex, national origin, ancestry, handicap, or familial status.
7. **B** Steering is the channeling of potential buyers to or away from particular areas as a means of discrimination.
8. **A** Redlining is the refusal to loan within an area.
9. **A** The illegal act of blind advertising is committed when advertising a property, and the licensee fails to disclose that the property is offered through a licensee.
10. **A** Failure to disclose this fact and provide the name of the licensee is called blind advertising and is illegal.
11. **A** Real estate law imposes this restriction on mobile home sales.
12. **A** All material facts pertaining to equipment requirements must be revealed. A permit from the Department of Transportation or local agency must be obtained.
13. **B** Brokers have that responsibility and the records must be kept for three years.
14. **A** The purpose of this monthly activity is to check that the money in the trust account is equal to their liability.
15. **B** The account must be a demand deposit account.
16. **A** This money is used to cover bank service charges.
17. **B** The brokerage firm owns all contracts.
18. **B** Employing brokers are responsible for supervision of all salespersons.
19. **A** The employment contract establishes the broker/salesperson relationship.
20. **B** Independent contractors set their own hours and pay their own taxes.
21. **A** Should the person answering the call indicate an interest in using the services of a broker, the person answering must be referred to a licensee.
22. **B** With the principal's consent, unlicensed sales assistants may greet the public and provide factual information by handing out preprinted materials.
23. **A** The CMA is subject to the approval of and is for use by the licensee.

24. **A** With the principal's consent, they may let into a property a person who is either to inspect or to perform work to the property. Only a licensee can show or exhibit the property to a prospective buyer.

25. **A** The commissioner is empowered by law to issue these regulations.

26. **A** This is part of the commissioner's role.

27. **B** Only the real estate commissioner can suspend, revoke, or deny a real estate license.

28. **B** The commissioner becomes the complainant, and the licensee is the respondent. The person who initiated the complaint is the witness.

29. **A** Failure to reveal a criminal conviction or disciplinary action that occurred at any time in the applicant's history on a license application may result in denial.

30. **B** It does contain 150 questions, and at least 70% of them must be answered correctly. Salesperson applicants have 3 hours 15 minutes to complete the exam.

31. **B** The term is four years, at which point it must be renewed.

32. **A** All courses must be approved by the Department of Real Estate.

33. **B** The Recovery Account is financed by license fees.

34. **A** The damages must be awarded by a court or as the result of an administrative proceeding and be noncollectible.

35. **B** A maximum of \$50,000 per transaction or \$250,000 per licensee can be paid from the Recovery Account.

36. **B** The license is suspended until the licensee repays the fund.

37. **A** It is a standard of conduct by which the individual guides her own behavior and judges that of others.

38. **A** It is designed to promote and maintain high standards of conduct in the transaction of the real estate business.

39. **B** Ethics has nothing to do with legality. Ethics deal with what is right. Laws set minimum standards for what a society regards as acceptable behavior.

40. **A** Regardless of race, color, sex, religion, ancestry, physical handicap, marital status, or national origin.

41. **B** Most of their technology needs are done through outside programs.

42. **A** A multiple listing service is an organization of real estate agents that receives information from members on their property listings and makes that information available to all participating members.

43. **A** The education requirements for certification will prepare licensees for more effective online communications.

44. **A** It is an alternative to storage on a computer's hard drive.

45. **B** Real estate brokers can be property managers, but sound business practice, as well as ethical considerations, require that they be adequately prepared before offering their services as property managers.

46. **A** Individuals must meet certain standards in order to earn the CPM designation.

47. **B** Every building of 16 or more units must have a resident manager. By living on the premises, the resident manager helps ensure that tenant complaints are handled promptly.

48. **B** The manager's compensation is based on the income the property produces.

49. **A** For example, some agents handle only restaurants, while others may specialize in office buildings, retail stores, or warehouses.

50. **A** But the dollar volume in these few sales tends to be high.

51. **B** Licensees often choose this specialty, although agents who handle primarily single-family home sales can also be involved with this specialty.

52. **A** However, the rent control board could further reduce rents for Health and Safety Code violations.

53. **B** Business opportunities can be listed and sold by real estate licensees with or without real estate.

54. **B** Many agents specialize in listing and selling lots for investment purposes, as well as to provide builders with a supply of land parcels of all sizes.

55. **A** Besides the sale of new time-shares, there is also a growing market in resales.

56. **A** Mortgage loan activities require a strong desire to meet the needs of others.

57. **A** The TDS is a form specified by law and prepared by the California Association of REALTORS®.

58. **B** The form should always be completed by the seller.

59. **A** Also exempt would be co-owner to co-owner sales, or other examples where the seller would not have knowledge of the property or would not need disclosure.

60. **A** Use of the form prepared by the California Association of REALTORS® is the best way for the seller and broker to be sure that the buyer is fully informed of the property's condition and that all legal requirements are met.

61. **B** It is required in residential transactions of one-to-four dwelling units.

62. **A** Exceptions include spouse transfers of title and co-owner to co-owner sale.

63. **A** The others are very high fire hazard zone, wildfire risk areas, and 100-year flood zones.

64. **B** Both the seller and the agent must sign the form.

65. **B** Only deaths on the property that occurred within three years of the offer to purchase are considered material facts and must be disclosed.

66. **A** The court held that a real estate broker has an affirmative duty to conduct a reasonably competent and diligent inspection of residential property and to disclose to prospective purchasers all facts revealed by the investigation and that materially affect the value or desirability of the property.

67. **B** Real estate agents owe to a third party a duty of full disclosure of material facts that the agent knows or should have known regarding the property condition.

68. **A** Under no circumstances is information regarding the escrow to be released to nonparties.

69. **B** It is thus in a real estate agent's best interest to not only make the appropriate property inspection and disclosure but also to be specific about what is not included in that inspection.

70. **B** The type of inspection necessary will depend on the type of property. Every property should have an inspection that includes the structure and mechanical systems.

71. **B** The home inspector's report will reveal any areas requiring further investigation.

72. **B** Who pays for this termite report depends upon the negotiation between the seller and the buyer.

73. **A** The escrow officer also obtains the necessary approvals of those reports by the parties.

74. **A** If the seller has agreed to pay for the indicated repairs through escrow, a provision for that payment at closing must be made.

75. **A** Thus, expanding home ownership opportunities for all racial and cultural backgrounds.

76. **A** This is a sound diversity strategy to incorporate into an overall business plan.

77. **B** The goal is inclusion. Everyone has the right to buy or rent real property.

## Multiple-Choice Questions

1. **B** Conversion is to change from one use to another, as in the case of misappropriating funds entrusted to a licensee. *Commingling* is mixing funds of the agent with those of the client, and failure to make full disclosure can be called negative fraud.
2. **B** The \$100 collected by the broker is an advance fee because the money to pay for it is collected from the principal in advance, distinguished from advertising in a newspaper and paying for the advertising after the fact out of the commission collected. By law, in order to avoid possible misuse or errors, such advance fees must be placed in the broker's trust account and expended only for advertising the property, and brokers must provide a report to the seller itemizing all expenditures made.
3. **D** Reconciliation is the balancing of the broker's trust account record with the balance as indicated on the bank statement.
4. **C** A trust account is set up as a means to separate trust funds from nontrust funds. A trust account protects principals' trust funds in situations in which legal action is taken against the broker or the broker dies or becomes incapacitated.
5. **C** Interpleader is a court proceeding by the stakeholder of property who claims no proprietary interest in it, for the purpose of deciding who among claimants is legally entitled to the property.
6. **B** The Real Estate Law permits a broker to hold the check when he has been ordered to do so by a principal. Because he was not authorized by the seller to accept a personal check, his acceptance of such a check makes him the agent of the buyer for the amount of the check.
7. **C** In both cases, there would be a violation of the fair housing laws.
8. **D** The Rumford Act prohibits discrimination due to race, religion, color, sex, marital status, physical handicap, national origin, or ancestry in the sale, rental, lease, or financing of housing. The California attorney general has ruled that these characteristics are not material facts and should not be disclosed.
9. **D** The Unruh Act covers the civil rights of persons in business establishments. By renting only to members of the Caucasian race, the broker is in violation of this act and is liable for actual damages plus \$250. The broker also would be subject to suspension or revocation of his real estate license.
10. **D** Discrimination is illegal, unlawful, and against public policy.
11. **A** The Real Estate Law prohibits any solicitation based upon the entry into a neighborhood of a person of another race, color, sex, religion, ancestry, physical status, marital status, or national origin. This practice is called *blockbusting* or *panic peddling*.
12. **B** Questions that deal with discrimination should be answered with a color-blind attitude and without bias. Any choice that hints at discrimination is probably the wrong choice. It is incorrect that you can lawfully assume the prospect is interested in a house in a minority neighborhood because although the house the minority prospect wants is in that neighborhood, it does not mean he wants the house because of its proximity to other minorities. Although it may be overreaching to assume the prospect desires a particular type of architectural style, it is not discriminatory.
13. **C** This is the law's basic purpose: to provide all persons in the United States with fair housing opportunities.
14. **A** A blind ad is advertising by a licensee who does not disclose in the ad that the property is offered through an agent rather than by the principal.

15. **C** Advertising of any service for which a license issued under provision of the Real Estate Law is required must at least set forth the name of a salesperson as an agent and their 8 digit DRE license number.

16. **A** Regulation Z of the Truth in Lending Act requires that all credit terms be mentioned in advertising. “No down payment” is allowed, but the other credit terms must be set forth. A seller is not an arranger of credit and not under the regulation.

17. **D** Of the choices given in this question, only the amounts of the different monthly payments would need to be disclosed in advertising.

18. **B** There are exceptions to Regulation Z. The truth-in-lending laws do not cover loans made to individuals for business or commercial purposes, and advertising homes sold “subject to” existing financing would not be covered by Regulation Z.

19. **C** The Real Estate Law requires that most documents be kept for a minimum of three years.

20. **C** The Real Estate Law dictates that the broker must keep a copy for three years starting from the date of closing, if such occurs. The date of the listing is used if the escrow does not close.

21. **D** Broker associates are people who have fulfilled all the professional and educational requirements to become brokers, but choose to go to work for another broker. Per California law, broker associates and real estate salespeople (collectively known as “associate licensees”) are considered the employees of the broker of record at their brokerage firm. The broker of record has a continuous legal duty to supervise associate licensees, no matter how much professional experience these associate licensees possess. A broker associate would not supervise the employing broker of record. The DRE does not supervise ongoing real estate activities of a brokerage firm, although it may, upon occasion, investigate them. Note: At a brokerage firm, associate licensees are general agents, acting on behalf of their employing broker (the principal).

22. **A** A broker may delegate her responsibility and authority (so long as the broker does not relinquish overall responsibility for supervision of the acts of salesperson licensed to her) to a real estate salesperson licensed to the broker if the salesperson has two years of full-time experience during the immediately preceding five-year period and has entered into a written agreement with the broker with respect to the delegation of authority.

23. **B** Only a real estate licensee is authorized to discuss features of the property, including the athletic programs at the local schools. Living nearby the subject property is not an exception to the rule. When Matthew Green answered questions about athletic programs at nearby schools, he was engaging in activities for which a real estate license is required. Being approved to sit for the DRE state salesperson’s exam means that Matthew Green is still unlicensed. Note: It was unlawful for Christina Green to permit her unlicensed assistant to engage in activities for which a real estate license is required, and may result in the revocation or suspension of her real estate license. The penalties for Michael Green may include a fine (of up to \$20,000) and/or a jail term (of up to six months).

24. **D** An unlicensed assistant, no matter how knowledgeable or experienced, is not permitted to explain transaction-related documents to a member of the public.

25. **B** The district attorney prosecutes violators of the Real Estate License Law. Without a license, one cannot receive compensation, a commission, or a fee for the performance of any of the acts defined as being within the purview of a licensed broker or salesperson. Because the person in the question is not licensed, the real estate commissioner would not have the authority to discipline this individual.

26. **D** Making any false promise of a character likely to influence, persuade, or induce; withholding facts that materially affect the desirability of property; or misrepresenting with the intent to induce a party to enter a contract would be fraudulent misrepresentation. The agent would be faced with the possibility of civil liability and disciplinary action by the Department of Real Estate.

27. **D** All of the items listed are violations of the Business and Professions Code—Sections 10177. This part of the Code includes areas or situations where the licensee was not necessarily acting as an agent.

28. **C** The commissioner may adopt, amend, or repeal rules and regulations reasonably necessary for the enforcement of the Real Estate Law. The commissioner may not create statutes; only the legislature has this authority. Civil courts settle disputes over commissions. The commissioner may not issue a license to operate in another state.

29. **C** A broker is responsible for supervision of employed salespersons. A failure to supervise salespersons, which might contribute to the salesperson's violation of laws, could lead to disciplinary action against the broker, as well as against the salesperson. Only the real estate commissioner can revoke a real estate license, never the court.

30. **C** Real estate commissioner's Regulation 1726 requires that every real estate broker have a written agreement with each employed salesperson and broker.

31. **D** The Department of Real Estate may take disciplinary action against an agent's license if the agent has been guilty of making any substantial misrepresentation.

32. **D** The broker could be disciplined for not notifying the commissioner of the violation, and the salesperson could be disciplined for receiving commissions from someone other than the employing broker.

33. **A** Only the real estate commissioner has the legal authority to suspend or revoke a license.

34. **D** An unrestricted license issued by the DRE for real estate brokers, broker associates, and salespeople is for a four-year term. "PRLS" stands for Prepaid Rental Listing Service: That license is issued for a two-year term. The PRLS license is required when charging a fee to supply prospective tenants with lists of available residential properties to lease. Note: While a real estate broker can obtain a PRLS license, it is not a requirement before that broker can lawfully engage in PRLS activities.

35. **B** A commission cannot be split with a licensee whose real estate license has expired. Because the salesperson did not complete the required continuing education before the expiration of the four-year license term, the employing broker of record will not be able to split a commission with this salesperson. If the salesperson does not complete the continuing education classes during the two-year grace period, the DRE will require the salesperson to retake the state exam. Per the DRE, the certificates issued upon successful completion of the three licensing classes are good for life: The salesperson will not have to repeat the three licensing classes.

36. **C** Both these dollar amounts are correct. The maximum amount the Consumer Recovery Account will pay applicants is capped at \$50,000 per transaction with an aggregate maximum of \$250,000 per licensee.

37. **C** The fact pattern states that the loss occurred as a result of a single transaction: The maximum the DRE will pay from the Consumer Real Estate Recovery Fund for a claim related to a sole transaction is \$50,000. Thus, the maximum the married couple would receive from the DRE is a total of \$50,000 (not \$50,000 each). The lifetime maximum the DRE will pay from the Consumer Real Estate Recovery Fund for one licensee with multiple claims from different transactions is \$250,000. The DRE Consumer Recovery Fund pays claims for intentional fraud, intentional misrepresentation, and theft (a.k.a. "conversion") of trust funds.

38. **D** Neither of these parties investigates or punishes acts of alleged unethical behavior of real estate licensees. Ethical behavior is treating others as you want to be treated. Unlawful activity, in contrast to unethical activity, is a violation of California law. The DRE investigates—and disciplines—illegal activity of real estate licensees. In the criminal court system, local district attorneys prosecute illegal activities, including those perpetrated by real estate licensees. Penalties imposed by the criminal courts include monetary fines, imprisonment, or both.

39. **A** Real estate licensees in California should—but are not legally required—to follow the NAR Code of Ethics. Note the difference between law and ethics. The law sets minimum standards of behavior: If people drop below this standard, they will be punished for acting illegally. The NAR Code of Ethics, in contrast, sets standards of behavior higher than those imposed by law with the goal of achieving conduct that is moral, right, honorable, and just. Violation of the NAR Code of Ethics will not result in discipline by the DRE, prevention of a real estate license renewal, or a restricted real estate license. The state DRE does not discipline real estate licensees for ethical violations.

40. **A** In order to gain e-PRO® certification, a real estate licensee must be a member of the National Association of REALTORS®, a nationwide voluntary association of real estate professionals. Only members of NAR can properly identify themselves as REALTORS®. Before becoming e-PRO® certified, a real estate licensee who belongs to NAR must complete a two-day course and pass an exam. The other answer choices are incorrect. The state DRE and federal HUD are government entities, both uninvolved in e-PRO® certification. The National Association of Real Estate Appraisers is a professional association for licensed real estate appraisers.

41. **D** When the tenant has breached the contract by not paying rent, the landlord must institute an unlawful detainer action in court. Part of this procedure is to give the tenant a three-day written notice and the action has to go through court.

42. **C** Assignment of leasehold means the entire interest is transferred and includes the remaining term and the entire premises. *Subleasing* is transferring part of the premises or less than the entire term.

43. **D** Regulation Z (of the federal Truth in Lending Act) does not apply to (a) business, commercial, organization, and agricultural credit (not notwithstanding any dollar amounts); and (b) credit over \$25,000 not secured by real property or dwelling. Regulation Z does apply to individuals and businesses who (a) offer or extend credit regularly that is (b) subject to finance charge or is (c) payable by a written agreement in more than four installments and is (d) primarily for personal, family, or household purposes.

44. **B** Surrender is a mutual agreement between the landlord and the tenant to terminate a lease. Rescission is a mutual agreement to release each other from any contract *before performance*, under which the parties must restore each other to their former positions.

45. **C** For every lease, the law implies a covenant (promise) on the part of the lessor (“owner of the paramount title”) to the “quiet enjoyment” and possession of the property by the lessee during the term of the lease. It is a warranty by the lessor against the lessor’s own acts, not those of strangers (neighbors and the like).

46. **C** A sublease is a transfer of less than the leasehold with the reversion in the sublessor and would create no form of title in the sublessee. A land contract transfers (1) possession, (2) equitable title, and (3) the right to acquire the fee title after all the conditions of the contract have been met. A mortgage does not convey any possessory interest; it is a security device.

47. **B** A landlord would not likely be found guilty of constructive eviction for failing to repair excessive wear and tear caused by the tenant. The three other circumstances would be classified as constructive eviction.

48. **D** Flashing is sheet metal (or sometimes composition material) that is used to protect, cover, and deflect water from joints or angles, such as roof valleys, or above window and door openings.

49. **C** A foundation plan shows the details of the foundation, which includes footings, piers, and subflooring.

50. **A** A franchise agreement is set forth in the Franchise Investment Law as: “A contract between two or more persons where one grants the other the right to sell, offer to sell, or exchange goods or services under a marketing plan designed by a grantor.”

51. **C** The first three choices are all grounds for discipline of a licensee. Under the provisions of Business & Professions Code Section 10131.6, licensees may “sell or offer to sell, buy or offer to buy, solicit prospective purchasers of, obtain listings of, or negotiate the purchase, sale or exchange of any mobile home if it has been registered.” There are no size limitations.

52. **C** Under common law, an estate at will is one that can be terminated at the will of either party without advance notice. The Civil Code of California, however, requires that any estate created by agreement, except an estate for years, requires advance notice to terminate. Therefore, an estate at will can be created only by operation of law in California.

53. **C** Under common law, an estate at will is one that is terminable at the will or unilateral decision of either party. By statute, California has modified the abrupt conclusion of such estates and requires advance 30-day notice of termination by each party. If this question had referred to common law, the answer would have been “none of the above.”

54. **A** The property is held by both spouses. She may file a homestead exemption of \$75,000. The property would not be sold because the \$519,000 loan and the \$75,000 exemption exceed the \$533,000 market value of the property.

55. **D** Most investors in real estate demand a greater return than is customary with bonds or trust deeds because the risk of ownership is higher and the investment does not have the same degree of liquidity.

56. **C** Real estate brokers are not allowed to list mobile homes that are “new,” which means those not registered with the DMV or H&CD. An exception is allowed if the mobile home is bought to be installed on a “regular” lot and is handled as real property by a proper recordation with the county recorder. When a manufactured home is properly installed on a permanent foundation on the owner’s lot, it becomes real property and is no longer a mobile home.

57. **B** The buyer does not complete the TDS. It is on behalf of the buyer that the other parties (i.e., seller, listing agent, selling agent) are required to complete their portions of the TDS. The TDS provides information to the prospective buyer of a residential dwelling of one-to-four units. A property with 5 or more units is considered commercial property, and the TDS is not required. The listing agent is the seller’s agent: If the seller does not have an agent, the listing agent portion of the TDS would be left blank. The selling agent is typically the buyer’s agent: If the buyer does not have an agent, the selling agent portion of the TDS would be left blank. If the listing agent is serving as a dual agent to both the seller and the buyer, the selling agent portion of the TDS is left blank.

58. **D** The Transfer Disclosure Statement (TDS) is required for the sale of residential property of one-to-four units. The TDS is completed by the seller (with certain exceptions) and any agents involved in the transaction. It must be given to the prospective buyer, as soon as practicable. However, the real estate described in this test question is a five-unit apartment building. Thus, the TDS would not be a legal requirement for this sale. Note: The information about lead-based paint is here to distract you from the actual question being tested.

59. **C** If a property lies within one (or more) of the following hazardous areas, that fact must be disclosed on the Natural Hazards Disclosure Statement: Special Flood Hazard Area, Dam Failure Inundation, Very High Fire Hazard, Wildland Fire Hazard, Earthquake Fault Zone, and Seismic Hazard Zone. Natural hazards are those that can cause damage without any human intervention. If a property is located in one or more of these zones, it can limit development and the ability to purchase insurance. Environmental hazards, on the other hand, are brought to the property through human intervention. Environmental hazards would include such things as asbestos, formaldehyde, radon gas, carbon monoxide, and mold. While mold and radon gas occur naturally, they become environmental issues in a building typically due to modern methods of construction and installation.

60. **B** The Natural Hazards Disclosure Statement is not part of the purchase contract between seller and buyer. It is a separate disclosure that the seller of a single-family residence is legally obligated to provide to the buyer. The Natural Hazards Disclosure Statement has nothing to do with government-guaranteed or -insured financing programs.

61. **C** Failure to disclose any material fact to the broker's principal is considered negative fraud and makes the broker subject to disciplinary action by the real estate commissioner. That a buyer is the broker's relative, friend, or close associate is a material fact because it could possibly influence the seller's decision in the sale.

62. **C** Real estate licensees can never misrepresent property values. This includes the practice of "buying a listing" by telling owner that their property is worth more than it really is in order to obtain the listing.

63. **C** The broker cannot use the statute of frauds as a defense in this situation. The statute requires that the listing contract be in writing to be enforceable in court but has nothing to do with misrepresentation.

64. **C** The action of the unlicensed assistant was illegal. An unlicensed assistant is only allowed to give information about a specific property when that information has been reviewed and approved by a real estate licensee, and the unlicensed assistant informs the recipient of this fact. Merely because the information had been reviewed and approved by the broker of record for a nearby property did not make it accurate for the subject property.

65. **B** The California DRE issues the Public Report on new subdivisions of five or more newly divided parcels, based on information received from developers. The Public Report is required by the Subdivided Lands Law, a consumer protection statute. The Public Report contains disclosures related to, among other things, compliance with applicable law, material disclosures, and the status of the project's financing. The information in the Public Report helps prospective buyers make informed decisions. It is also intended to prevent fraud, misrepresentation, and deceit being perpetrated by developers upon the public. This law is administered at the state—not the municipal—level by the DRE.

66. **A** A prudent seller, after consulting with the broker, obtains a structural pest control inspection report before putting the property on the market. The report can help in determining the pricing of the property.

67. **B** The results of a pest control inspection report, including the cost of corrective work, would be material facts to a buyer and must be disclosed. If two or more inspections are made, all reports must be disclosed.

68. **C** Both federal and state fair housing laws prohibit discrimination on the basis of race in the sale or leasing of real estate. If the real estate licensee helps the roommates find an additional roommate of a different race, the real estate licensee would violate both federal and state fair housing laws. Why? Because compliance with the request of the three current roommates would result in the automatic exclusion of any prospective tenant who belongs to a race of a tenant already living in the apartment. Note: The shared living area exception applies to sex, not race (e.g., a female roommate in an apartment with shared living areas can advertise for a female roommate).

69. **A** Eviction of tenants for no reason other than that they have been victims of domestic violence may result in liability on the part of the landlord. Here, the victim of the domestic violence—not the perpetrator—may well have a basis of a lawsuit against the landlord for the eviction notice. The warranty of habitability is implied by law in every residential lease in California. The warranty of habitability is a legal requirement imposed on residential landlords to keep leasehold property in livable condition. An uninhabitable property would, for example, lack heating, plumbing, and/or electricity. There is nothing in the fact pattern to suggest a breach of the warranty of habitability.

6. **B** Demand is determined by the number of potential purchasers.

7. **B** Transferability is the ability of the seller to convey good title to the buyer.

8. **B** The highest and best use is the use that produces the greatest return over time.

9. **A** Future benefits determine the current value.

10. **B** Price moves opposite of supply; when supply goes up, price goes down.

11. **B** Substitution is the basis of the sales comparison approach.

12. **A** Regression is when the value of overimproved property declines.

13. **A** In an appraisal, a property improvement is valued at only its contribution to the property's market value.

14. **B** Decreasing returns are improvements that add less value than they cost. An example would be a swimming pool.

15. **B** Identifying the problem is the first step in the appraisal process.

16. **B** There are three. The sales comparison approach, the cost approach, and the income approach.

17. **A** The sales comparison approach is also called the market data approach and market comparison approach.

18. **A** The estimate of value is based on adjusted sale price of similar properties that were recently sold.

19. **B** Never adjust the price of the subject property. Adjustments are made to the comparables.

20. **A** Adjustments are always made to the sold comparables to make them similar to the subject property.

21. **A** The cost approach is typically used when comparable sales or income is lacking.

## Unit 6

### True/False Questions

1. **A** A real estate appraisal is an estimate of value as of a specified date supported by an analysis of relevant property data.

2. **B** All real property appraisals must be performed by licensed appraisers.

3. **A** This value is objective, because it is not based on the requirements of a particular buyer.

4. **A** Market price is a historical fact and the actual price paid in a transaction.

5. **A** Utility is subjective, based on the needs and desires of a specific potential buyer.

22. **A** In the cost approach for establishing value, the appraiser determines what it would cost to duplicate the subject property.

23. **A** It is the cost to build a replica of the subject property.

24. **B** Economic obsolescence is associated with factors external to the property, such as a flight path from a nearby airport. Wear and tear is related to physical deterioration.

25. **A** Examples are apartment buildings, shopping centers, or residential rental property.

26. **A** Potential gross income is a property's maximum income from all sources.

27. **A** The cap rate is the property owner's annual expected rate of return.

28. **B** Effective income minus operating expenses equals net operating income (NOI). Debt service is subtracted from NOI to arrive at cash flow.

29. **B** Contract rent is the rent received by the current property owner. Market rent is an estimate of the property's rent potential.

30. **B** Contract rent may be higher or lower than market rent.

31. **A** The appraiser estimates and then subtracts these anticipated losses from gross income to derive effective gross income.

32. **A** Effective gross income minus operating expenses equals net operating income (NOI).

33. **B** Net operating income divided by capitalization rate equals estimated market value.

34. **B** The cap rate is the property owner's annual expected rate of return.

35. **A** The capitalization rate can be expressed as the relationship between the net operating income the property produces and its market value.

36. **B** The cap rate can be developed by analyzing net income and sales prices of comparable properties.

37. **B** Better investment properties have lower cap rates due to their lower risk factors.

38. **A** Interest and principal payments are considered costs associated with a particular buyer rather than with operating expenses of the property.

39. **A** The gross multiplier is called the gross income multiplier or the gross rent multiplier.

40. **B** Monthly gross multiplier is generally used for residential property. Because its income is generally limited to rent, the multiplier for a single-family residence is usually termed a gross rent multiplier.

41. **A** The gross income selected by the appraiser for the subject property is multiplied by rental income to arrive at market value.

42. **A** Front foot is a measure of frontage used in appraising commercial property.

### Multiple-Choice Questions

- B** This example is based on the principle of progression.
- C** When effective demand remains the same, if supply decreases, prices rise.
- B** The terms *expenditure* or *sacrifice* mean the same. Cost is a measure of past expenditure or sacrifice; maintenance cost is the present expenditure or sacrifice; and value is the measure of the present worth of future income.
- D** On a given site, some amount of capital investment on improvements, furnishings, or service rendered in management, the maximum return is reached and additional amounts will yield decreasing rates of return on the investment. This is an application of the appraisal principle of increasing and decreasing returns.
- B** The economic life is the period in which the building earns sufficient income to support itself. The building will still be standing even though its economic life may have expired.

6. **A** The principle of substitution states that when several similar commodities, goods, or services are available, the one with the lowest price attracts the greatest demand and widest distribution.

7. **C** Applying the principle of conformity, value would be upheld or stabilized if most of the homes in the neighborhood were owner occupied. The rate of turnover would be affected by other economic factors relating to the employment of the residents.

8. **D** Although private restrictions affect real estate value, they are not one of the four great forces. The four great forces are physical, social, economic, and political.

9. **A** Greater depth will add to the value of the lot; therefore, “there is no difference in value” and “the total value of the lot would be less” are false. Greater depth decreases square-foot value; therefore “the square-foot value increases” is false. “The front-foot value increases” is the only true statement.

10. **B** The economic life of property is the period of time over which improvements to real property contribute to property value.

11. **C** Amenities are the attractive or desirable features of a home or a neighborhood. These may be physical attributes or perhaps the neighborhood’s attitude toward schools, well-kept lawns, et cetera. These may be tangible or intangible qualities measurable on the market.

12. **C** Newness in itself would not be a stabilizing influence. Zoning regulations and private restrictions generally have as their primary function the protection and stabilization of property values. Availability of public transportation has always been a significant factor influencing property values in most residential areas.

13. **C** The roof described is a hip roof.

14. **A** Economic obsolescence is a loss in value due to factors outside of the subject property that adversely affect its value.

15. **B** The land residual technique of the income approach is used to determine the value of the land.

16. **B** There is an inverse relationship between capitalization rates and property value. As the cap rate goes up, the value of the property goes down. As the cap rate goes down, the value of the property goes up.

17. **B** Comparable sales data for estimating the value of land should be used whenever possible.

18. **A** The principle of substitution asserts that the market value of a property is set by what it would cost to find an equally desirable substitute property. In the comparative analysis method, the selling prices of comparable properties would indicate what buyers are willing to pay for similar properties. (The principle of substitution may be used in all three appraisal methods.)

19. **C** Misplaced improvements and change in directional growth pattern would contribute to economic obsolescence; massive cornices on an apartment building would contribute to functional obsolescence. Normal wear and tear is physical deterioration, not obsolescence.

20. **B** The comparative analysis or market data approach to appraisal is the easiest way to value land.

21. **C** Comparable sales data (also known as comparable *market* data) are the data on which appraisers rely for site analysis and valuation. There are many kinds of market information, but sales are still the foundation of appraising methodology.

22. **B** Among the choices presented, gross scheduled income would yield the maximum possible income an income property can yield. “Scheduled income” represents the rent currently in effect on the property in question as if the property were fully occupied. If the property has space available, the gross scheduled income would be at the rent levels currently obtainable for the space in the local market. This represents the maximum income the property could achieve.

23. **D** The beginning or cover letter in a narrative form of appraisal sets forth the purpose of the appraisal and the final opinion of value. Everything that follows in this most comprehensive form of appraisal is the appraiser's data to support the appraiser's conclusion.

24. **C** The economic life is the period in which the building earns sufficient income to support itself. The physical life is how long the building will remain standing, which is typically much longer than the economic life.

25. **A** Depreciation can be from either inherent (inside) or extraneous (outside) factors.

26. **C** The letter and form types of appraisal reports are abbreviations or variations of the complete narrative form of report. The narrative appraisal report gives the appraiser the opportunity to support opinions and conclusions. The paragraphs mentioned in this question are generally included in the narrative report.

27. **C** For appraisal purposes, mortgage payments and income tax are not allowable deductions to arrive at net operating income. Depreciation adjusts the cost basis but is not an expense for appraisal purposes. Wages paid for gardeners and maintenance personnel are deductible from gross income as operating expenses.

28. **D** The *purpose* of the appraisal determines the type of value being sought. It is not the same as *function* or use. The function of the appraisal is the reason for which the appraisal is made or is intended to be used. It relates to the character of the decision to be based on the appraisal, for example, price at which to buy or sell, amount of mortgage to be made, et cetera. The appraiser under the *Uniform Standards of Professional Appraisal Practice (USPAP)* must state the intended use of users.

29. **D** Because of the action of the sun, the southwest sides of the street are best. Therefore, the northeast sides of the street are the least desirable corner of the street.

30. **D** The process of capitalization is "dividing net income by a percentage rate of return to determine value." The capitalization rate is the relationship between value and net income, not net worth.

31. **B** For determining net income in the income approach to appraisal, mortgage interest is a personal expense of the owner, not an operating expense of the property. Vacancies, management fees, and maintenance costs are all allowable deductions in establishing net operating income for appraisal purposes.

32. **D** Economic obsolescence is a loss in value due to factors away from or outside of the subject property. Additionally, the appraiser must look at the fact that the property in question overfunctions for the area. It is rare to have only one factor affect the property value. This is a good example of two types of obsolescence impacting the property.

33. **A** Effective gross income is that income remaining after deducting vacancies and collection losses from gross income.

34. **B** Submitting false information to a lender for the purpose of inducing the lender to make a loan is a felony. The Office of Real Estate Appraisers (OREA) could also remove the appraiser's license.

35. **C** Before making an appraisal, an appraiser must define the problem to see what is to be done and how it is to be accomplished.

36. **D** Reconciliation is the final step by the appraiser in any appraisal and is the act of bringing together conclusions in a short, concise statement (it can also be called summation). The terms *sales*, *comparative*, and *comparable* are used in the sales comparison approach.

37. **C** Vacancy factors will vary from time to time but can be estimated with accuracy.

38. **D** The buyer and the seller agree on a price, and the contract is signed. This would indicate the market value of property on that date. Values taken at any later date would defeat the willing seller-willing buyer concept.

39. **D** If there is an existing structure on the property, the appraiser will value the land for its highest and best use as if vacant, but must allow a reduction for the cost of removal of the structure.

40. **D** Economic rent is defined as the rent expectancy if the property were available at the time of its appraisal. The amounts the owner actually receives in rents and payment for the use of property designated in a lease relate to *contract rent*.

41. **B** In the analysis of a commercial district, the emphasis is on the quantity and quality of purchasing power available to the shopping area.

42. **C** All of these items would be added to the buyer's cost basis (book value).

\$30,000 down payment
\$60,000 assumed loan
\$2,400 delinquent taxes
\$2,250 commission (50% of \$4,500)
\$1,150 closing costs
\$95,800 total

43. **D** Unearned increment is an increase in value of real estate due to no effort on the part of the owner; it is often due to an increase in population or inflation. Amenities may or may not be due to the owner's effort.

44. **D** Appraisal fees are set by agreement between the appraiser and the client.

45. **B** *USPAP* stands for *Uniform Standards of Professional Appraisal Practice*.

46. **B** A fee appraiser is one qualified by education, training, and experience who is hired to estimate the value of real and personal property based on experience, judgment, facts, and use of formal appraisal processes and is paid a fee for such services. A fee appraiser must now be state licensed or state certified.

47. **A** The owner would apply the principle of contribution. He must be sure that the investment in the improvements will produce sufficient additional income to cover the expenditure. If the net income increases adequately, he should go ahead with the plan.

## Unit 7

### True/False Questions

- B** The chain of title is a history of successive ownership documents linked together.
- A** Small issues such as a nonrecorded name change may be corrected with a quitclaim deed. Larger issues may require a suit to quiet title.
- B** The CLTA is called the owner's policy. The extended or ALTA policy is the lender's policy.
- A** This policy is intended primarily for the benefit of the lender.
- B** The grantor makes two implied warranties in executing a grant deed. The grantor warrants that the grantor's interest in the property has not already been conveyed, and there are no undisclosed encumbrances on the property, such as tax liens.
- B** Delivery and acceptance are the two requirements for a valid deed to be effective.
- B** The quitclaim deed is a commonly used way of clearing a cloud on title.
- B** An escrow also can help in a transaction involving personal property, including what is known as a bulk sale.
- A** If the escrow instructions differ from the terms of the underlying agreement, such as a purchase contract, the most recent in time controls.
- A** By this action, the escrow holder forces the parties to have their rights and obligations clarified in court.
- B** The escrow can be canceled, only if both parties provide written instructions.

12. **B** 1% of base year value is the maximum annual tax on real property.

13. **B** Assessed value is the property value to which the tax rate is applied. Assessed value increases annually by an inflation factor of no more than 2%.

14. **A** It runs from July 1 through the following June 30.

15. **A** A special assessment appears as a separate entry on the property tax bill.

16. **B** It is 55 cents per \$500 or fraction of \$500 of the consideration or sales price.

17. **A** This law expanded the type of facilities and services that could be provided by improvement bonds and also eliminated the requirements that improvements specifically benefit individual properties.

18. **B** The homeowner's exemption is \$7,000.

19. **A** Probate is the judicial process that determines the decedent's heirs and creditors, pays debts owed by the estate, and transfers title to any remaining property from the decedent to the decedent's heirs.

20. **A** The deceased is the legator, and the person receiving the property is the legatee.

21. **B** The probate court determines the commission.

22. **B** Ownership in severalty is ownership by one person. The root word is *sever*.

23. **A** Tenants in common may take title at different times and may own equal or unequal shares. For example, owner A owns 70% of the property, and owner B owns 30%.

24. **A** This means that when a cotenant dies, the survivors receive the deceased's share.

## Multiple-Choice Questions

1. **D** A local title company would have on record, as part of its business, all the information requested by Kale. The county engineer, real estate commissioner, and county planning commission would have only the information in their specialized fields.

2. **A** Although the standard coverage policy is limited in coverage, most buyers accept this type of policy when they purchase real property.

3. **D** A title insurance company will insure the validity of a lease and an encumbrance by the use of a special endorsement, and insure against losses from restrictions known or believed to be unenforceable.

4. **D** In a grant deed, there is an implied warranty that the property being conveyed is free from all encumbrances known to the grantor, other than those disclosed to the grantee.

5. **B** The stem of this question gives us a good definition of abstract of title. The part of the question that suggests *abstract of title* rather than *chain of title* is the phrase "facts relied on as evidence of title."

6. **B** The best and most common protection to ensure title to real property is afforded by means of a title insurance policy.

7. **A** The law construes that everyone is given constructive notice when a document affecting title to real property is recorded where it can be seen by anyone. Recording gives constructive "notice to the world." Actual notice is expressed information of fact experienced by the person to whom given.

8. **C** Delivery is controlled by the intention of the grantor.

9. **B** The first to record, providing that person has no actual or constructive notice of any previous transaction, is the first in right.

10. **D** Smith will probably be unsuccessful in having the deed set aside if the claim is based on the fact that the deed was never delivered. The courts presume that a deed that is recorded was delivered. Although it is true that the deed is valid without recording, that is not the answer to the question asked.

11. **A** The grantor is the owner of whatever rights are to be conveyed, whether by grant deed or quitclaim deed.

12. **C** Recording a deed gives constructive notice to the world of the contents of the deed. The recording laws were enacted to protect innocent third parties. In this instance, the grantee did not record the deed; therefore, she cannot expect the courts to protect the title against third parties or subsequent recorded interests that have no knowledge of the document. The deed itself is valid between the grantor and the grantee, but invalid as against an innocent purchaser without notice.

13. **B** To alienate means that title is conveyed from one owner to another. Alienation is the opposite of acquisition.

14. **A** *Acquisition* is the act of acquiring; *alienation* is the act of transferring or conveying title.

15. **A** Establish the two dates and the time differential:  
COE May 1  
DI July 1 (taxes for the current fiscal year had been paid)  
Differential 2 months  
The date of the item (DI) is beyond the close of escrow (COE), so the buyer owes. Figure the monthly cost of the item and multiply by the differential.  

$$\begin{aligned} \$1,380 \text{ annual tax} \div 12 &= \$115 \text{ monthly tax} \\ \$115 \times 2 \text{ months} &= \$230 \text{ buyer owes to seller} \end{aligned}$$

16. **C** The escrow agent serves as agent for both until their transactions are carried out by delivery of the deed and other considerations. After closing, the escrow agent may act separately for either party.

17. **D** All real estate transactions, including the sale of one's own home, must be reported to the IRS. The primary reporting responsibility falls to the person responsible for closing the transaction (e.g., the escrow company or title company, if there is one). If there is no person responsible for the closing, the responsibility falls, in order, to the primary mortgage lender, the seller's broker, or the buyer's broker.

18. **C** The term *recurring costs* describes the expenses that the buyer can expect year after year. These include property taxes and fire insurance, which are frequently impounded by the lender.

19. **B** The proration of prepaid taxes will be a credit to the seller (and a debit to the buyer) because the buyer will be in title and benefit from that prepayment. Proration of prepaid rents will be a debit to the seller (and a credit to the buyer) because the seller will not be in title during the period for which the prepaid rents were paid. Cash charge for recording buyer's deed is a buyer's expense and therefore a debit to the buyer only. Cash charge for a quitclaim deed will be a seller's expense and therefore a debit to the seller only.

20. **C** A real estate broker who is not a party to the transaction would not be exempt from the regulations of the corporations commissioner. A broker who is an agent for one of the parties to the transaction may handle the escrow without being licensed by the corporations commissioner, whether the broker charges a fee or not. (Other exemptions include attorneys, banks, savings and loans, title companies, and related entities.)

21. **A** While escrow procedures vary somewhat according to local custom, one of the steps that comes after preparing escrow instructions, ordering the title search, and accepting the structural pest control reports is for the escrow officer to call for the closing funds that are deposited into the escrow. The escrow could not authorize work to be done, change the broker's commission, or tell the buyers where to obtain financing.

22. **C** Taxes, and interest in an assumption, are usually prorated in escrow. If the seller's insurance is taken over by the buyer, the seller will be credited proportionately (pro rata) for the portion of the premium the buyer is debited for. When the buyer gets new insurance, the seller's policy will be canceled and the premium returned to the seller by the insurance company short-rated on a uniform schedule approved by the insurance commissioner.

23. **D** An exchange merely defers the taxes and is not truly tax free. The benefiting party acquires another property and any profit upon its eventual sale will result in a tax.

24. **C** Sales tax would be charged on trade fixtures and furniture, but not on intangible assets such as goodwill, the accounts receivable, or stock-in-trade for resale.

25. **D** The taxes have been paid to July 1, 2014, which is three months short of the close of escrow, September 30, 2014. The seller is obligated to pay the buyer for the taxes for the months of July, August, and September.

1. C.O.E.: September 30, 2014
2. D.I.: July 1, 2014\* \*Date of item: Taxes paid to July 2014
3. Short of C.O.E. 3 mos. Therefore, seller owes 3 mos.

26. **A** Cost basis is the same as tax basis. The addition of a capital improvement would constitute an increase to cost basis.

27. **C** Straight line, sinking fund, and sum-of-the-years' digits are all accepted methods of providing for depreciation. Obsolescence is not a method, but a type of depreciation.

28. **D** The most complete and accurate statement for adjusted basis is acquisition cost plus capital improvements minus depreciation.

29. **C** Depreciation reduces the original cost basis, thereby increasing the difference between the selling price and the new (or "adjusted") cost basis. That difference is a long-term capital gain on which the taxpayer will pay taxes. In this case, Smith's gain equaled the depreciation taken.

30. **B** Between March 1 and July 1, the county tax assessors compile a list showing the assessed value of all taxable property in the county (the tax rolls) as of March 1. This total is the tax base. Using this, and the budget to run the county, the board of supervisors sets the tax rate needed to meet the budget, within the limits set by Proposition 13. The county tax collector applies the rate to each property's assessed value to determine that year's individual property tax.

31. **A** If points are paid to a lender solely for the use of the money borrowed (discount points), they may be deducted in full by the borrower as an interest expense. If they are paid for specific services of the lender, they are not deductible as interest. Points paid for interest are not always deductible if paid for interest; an example of an exception is points paid by a seller.

32. **C** Boot is something that is not of a like-kind received in a tax-deferred exchange. It includes cash or equivalent, such as a note and trust deed, other personal property, and net debt relief (mortgage relief). It is unrelated to depreciation.

33. **A** To be eligible for a Section 1031 exchange, a property must be held for income or investment or be property held for productive use in trade or business. "Each party must trade for like property of equal value with a smaller mortgage and receive boot" is incorrect because boot would not be received in the trade for property of equal value with a smaller mortgage. "A party to the exchange can deduct a loss on the exchange" is incorrect because the loss is not attributable at time of exchange. "A rented house cannot be exchanged for an office building" is incorrect because rental property can be exchanged for an office building.

34. **B** A married couple is currently entitled to a maximum exclusion from capital gains of \$500,000. There is no limit on the number of times a couple or an individual can take this exclusion as long as they meet the current IRS requirement.

35. **D** Original cost \$300,000 to acquire property  
Recaptured -110,000 by sheltering her income from tax ("took depreciation" or recapture of investment)  
Remaining book value \$190,000  
Sold for \$300,000  
Less cost basis - 190,000  
Equals total \$110,000 long-term capital gain  
Note: In this example, by coincidence the long-term capital gain is the same as the amount of the depreciation taken.

36. **C** Smith can prorate the gain over the term of the installment contract.

37. **B** A quiet title action is the customary and appropriate remedy to establish the fact of forfeiture and to eliminate the contract interest of record.

38. **A** A quiet title action is "a remedy, originating in equity, having for its purpose an adjudication that a claim of title to or an interest in property, adverse to that of the plaintiff, is invalid, so that the plaintiff and those claiming under him may be forever afterward free from any danger of the hostile claim."

39. **C** Recording gives constructive notice of the contents of recorded documents. Anyone is presumed to have knowledge of what is contained in the public records, even if they have not inspected them.

40. **D** Prescription is a means of acquiring an easement in another's property and gives the easement holder a right to use the land. Title to the property is acquired through adverse possession.

41. **C** It is unnecessary to pay the taxes in order to acquire a prescriptive easement. Payment of taxes is necessary for adverse possession.

42. **D** A real property sales contract may not be transferred by the owner unless accompanied by a transfer of the legal title, and legal title may not be transferred by the owner unless accompanied by the assignment of contract. If the sales contract is not recorded, written permission by the vendee must be obtained to further encumber in an amount that together with the existing encumbrances exceeds the payments on the contract.

43. **A** A bill of sale is a written instrument by which one person sells, assigns, or transfers an interest in personal property to another.

44. **D** A grant deed carries a warranty to the purchaser; a land contract does not. The grant deed requires the signature of the grantor only; a land contract requires the signature of the vendor and the vendee. A grant deed does not require a designation of the price; a land contract does.

45. **B** Recording gives constructive notice "to the world," and anyone dealing with the property has constructive notice even though the public records have not been inspected.

46. **A** Generally, recording establishes the priority of a trust deed. "First to record is first in right." An exception would result from the existence of a subordination clause. Other exceptions may exist in relation to mechanics' liens and judgment liens.

47. **A** Any separate property (or tenancy in common interest) passes as follows: spouse and one child: each receives half; spouse and two or more children: one-third to spouse and two-thirds among children.

48. **B** *Executrix* is a female ("ix") named in a will to carry out its provisions as to the disposition of the estate of the deceased. "Executor" in modern usage can mean man or woman.

49. **C** A prisoner is not automatically deprived of his civil rights (including his right to contract or deed his property) unless he has been sentenced to death or to life in prison.

50. **C** Ownership of a property by one individual or one entity is an estate in severalty. Because Janet Lim is the sole owner of a parcel of real estate, she has an estate in severalty. The other choices show multiple, concurrent owners of a parcel of real estate.

51. **A** Ann's interest in the property will go to the surviving joint tenants. Holding title in a joint tenancy overrides the provisions of a will. If Ann wanted to leave her interest in the property to her child, Ann should have broken the joint tenancy before drafting the will. Note: Ann could have broken the joint tenancy as to her interest: Ann could not have broken the joint tenancy as to the interests of the other joint tenants (Ben, Cam, and Dan). The laws of intestate succession determine the distribution of someone's assets in the event that person dies before making a will. The fact pattern specifies that Ann executed a will before dying. Apart from the property held in a joint tenancy, a properly executed will determines how the deceased person's assets will be distributed.

6. **A** The owner of a life estate has the right of possession and use of property, but the estate lasts only as long as the life of a person identified in the deed.

7. **B** The term *metes* refer to distances and *bounds* are natural or artificial boundaries.

8. **B** The property owner receives compensation based on an appraisal, which is usually the property's fair market value.

9. **A** If no claimant comes forward within five years, title to the property vests in the state.

10. **A** An example would be a zoning change from multifamily use to single-family use.

11. **A** Since 1978, the use of lead-based paint in housing has been prohibited by the federal government.

12. **A** Homeowners associations frequently make use of deed restrictions to ensure that the uniform appearance of the homes in a subdivision is maintained.

13. **B** Riparian rights belong to owners of land bordering a river or other flowing stream. They do not own the water but have the right to reasonable use of it on their own property.

14. **A** Owners of littoral rights also have the right to make reasonable use of the water.

15. **B** In a stock cooperative, the land and the building are owned by a corporation. Owners receive corporate bylaws, shares of stock, and a proprietary lease.

## Unit 8

### Property Ownership and Land Use Controls and Regulations

#### True/False Questions

1. **A** Personal property becomes real property by attachment. Real property becomes personal property by severance.
2. **B** Subsurface rights include solid minerals, oil, and gas.
3. **A** The five tests for a fixture are method, adaptability, relationship, intent, and agreement.
4. **B** An encroachment is the unauthorized use of another person's land. A license is the revocable permission to use the land of another.
5. **B** A fee simple absolute estate lasts forever. A fee simple defeasible lasts so long as a condition is not broken.

## Multiple-Choice Questions

1. **A** Despite its weight, the 1,000-pound grand piano is considered movable personal property (a.k.a. “chattel”). Personal property is not shown as an exclusion in the purchase contract for real estate because it can legally be removed by the seller before the close of escrow. Only items that are affixed to the real estate—and are considered a part of the real estate—need to be excluded from the purchase contract when the seller wishes to keep them following the closing. The other items are considered part of the real estate and were properly excluded from the purchase agreement with the buyer.
2. **D** None of these activities are illegal. Purchasing title insurance is not a legal requirement. It is customary in California, however, for a seller to purchase an owner’s policy of title insurance for the buyer. A basic insuring clause in a title insurance policy is access to a street or road: The title company probably would have discovered the property lacked a legal right of access to a road prior to the transfer. It is also customary—rather than a legal requirement—to use an escrow company to assist with a purchase transaction of real estate. Escrow, however, is legally required for a transaction when it involves the sale of bulk goods as defined by the UCC; the transaction includes the sale of a liquor license; or the property is being sold through the probate court. It is also legal to sell landlocked property, provided the parcel is not in violation of some other law, like the Subdivision Map Act. Finally, in contrast to an easement, a license can be revoked by the property owner at any time.
3. **D** There is a split between legal title and equitable title for all these answer choices. In a deed of trust, the trustor (the borrower) holds equitable title. The borrower conveys bare legal title to a third party (the trustee). The trustee holds bare legal title on behalf of the beneficiary (the lender) until the loan is paid in full. Under a living revocable trust, the trustee (the caretaker of trust property) holds legal title, while the beneficiary (the party able to benefit from trust property) holds equitable title. Under a land contract, the seller (the “vendor”) holds legal title, while the buyer (the “vendee”) holds equitable title. After the land contract is paid in full, the seller will give a deed to the buyer who will thereafter hold both legal title and equitable title. Note: Legal title is transferred from grantor to grantee via a deed. Equitable title is the right to possess, use, and enjoy the subject property.
4. **B** A section of land in the U.S. government survey system is a one-square-mile area of land, containing 640 acres. The other answers are incorrect: The answer choice that states “5,280 feet” describes a distance, not an area of land, and therefore could not contain any acreage. The answer choice that states “one-half square mile, containing 320 acres” describes half of a section. The answer choice that states “one-fourth square mile, containing 160 acres” describes a quarter of a section.

5. **B** In the event of a default, senior liens are paid before junior liens. Usually, a lien that recorded first will be senior to any more recent or junior liens. However, because the priority of a mechanic's lien dates back to the first day when labor was performed or materials were delivered to a property (and not the date when the lien recorded), the mechanic's lien will need to be paid from the foreclosure proceeds before the foreclosing trust deed. Lenders make every effort to protect their lien priority, but because mechanics' liens jump to the first day labor was performed or materials delivered to the subject property, this type of event is a possibility. The other answers are incorrect: Property taxes and special assessments are one of the fundamental powers of government over owners of real estate. These are always in senior position over other liens. Thus, the foreclosing trust deed will always be junior to property taxes and special assessments. In the (unlikely) event that there is insufficient money to pay off both the outstanding property taxes and the outstanding special assessments, property taxes will be paid first.

6. **B** The owner did not violate the federal lead-based paint law: Federal law requires prospective buyers—not prospective tenants—be given a 10-day window to test for lead-based paint. The other answers are incorrect: The DRE only disciplines real estate licensees. The question states the owner does not have a real estate license. Actual knowledge is not required when providing prospective buyers with a 10-day window to test for lead-based paint in target housing (i.e., housing constructed before January 1, 1978). Finally, because it is not a legal requirement to give a prospective tenant a 10-day opportunity to test for lead-based paint, the real estate broker would not be sued for inadequate advice pertaining to this specific issue.

## Contracts

### True/False Questions

1. **B** This is the definition of a voidable contract.
2. **B** A minor becomes emancipated by marrying, joining the armed forces, or petitioning the court and thus becomes legally capable of entering into a contract.
3. **A** Net listings are illegal in a number of states, but legal in California. However, serious conflict of interest problems can arise.
4. **A** To exercise the option, the agent would have to reveal all offers received.
5. **B** Real estate agents now have duties to know about property offered for sale.
6. **B** The Easton case which determined that the agent has an affirmative duty to find out material facts only applies to residential property of one to four units.
7. **A** The three steps required to establish consent in a contract are offer, acceptance, and communication of acceptance.
8. **A** If either party changes any of the contract terms, they are making a counteroffer.
9. **B** Also known as an alienation clause, the due-on-sale clause calls for the promissory note to be paid in full upon sale of the property.
10. **A** The rate of interest individuals can charge for loans to purchase, construct, or improve real estate cannot exceed 10% or 5% greater than the rate designated by the Federal Reserve Bank of San Francisco to member banks for advances.
11. **B** This is the definition of an option. In an exchange, owners of different properties transfer title to each other.

12. **B** Until they are disbursed, they remain the funds of the principal from whom they were collected. Advance fees must be deposited into a trust account.

### Multiple-Choice Questions

1. **A** An offer is terminated if either the offeror (i.e., the party making the offer) or the offeree (i.e., the party receiving the offer) dies before the communication of acceptance. Note: A valid offer can be made on a property that is not currently listed for sale.

2. **C** In a double net lease, the tenant pays a base rent plus two expenses (e.g., taxes, insurance, maintenance) charged to the property. This would be more advantageous to the landlord than a net lease where the tenant pays a base rent plus only one of the property's expenses. Net leases are typically used for commercial properties. A gross lease (a.k.a. a "fixed lease") occurs when the tenant pays a fixed amount of rent and the landlord pays all expenses. Gross leases are typically used for residential properties, and are less advantageous to the landlord than a double net lease. A land or ground lease is for vacant land. The question states that the real estate is improved with a building.

3. **C** The buyer's consideration was the promise to pay the agreed-upon purchase price. Here are the essential elements of a valid contract: consent, capacity, consideration, lawful objective (Memory aid: Co-Ca-Co-La). These elements must be satisfied at the time of contracting. Consideration can be anything of value, including money or promises. A purchase contract is a bilateral contract between a buyer and a seller. "Bi" means two. A bilateral contract is a contract where the two parties satisfy the element of consideration by exchanging promises. In a purchase contract, the seller is promising to convey title to the buyer, and the buyer is promising to pay the entire purchase price to the seller. This exchange of promises happens at the time the parties enter the purchase contract, thereby satisfying the contractual element of consideration. The actual payment of the purchase price typically happens sometime in the future when escrow closes.

4. **D** Under California law enacted in 2009, no one can charge or collect an advance fee for loan modification or loan forbearance (i.e., "forgiveness") work.

### Financing

#### True/False Questions

1. **A** The Fed regulates the flow of money and the cost of credit to help stabilize the market fluctuations that create inflation and recession.

2. **B** In a fully amortized loan, equal payments including both principal and interest are made over the loan term such that the balance becomes zero with the last payment. In a straight note, the entire principal is paid in one lump sum at the end of the loan term.

3. **B** These are all part of the primary mortgage market. The secondary market is where promissory notes are bought and sold.

4. **A** The VA guarantees lender against loss on loans to veterans.

5. **B** In a mortgage, the borrower is the mortgagor and the lender is the mortgagee.

6. **A** Kickback are unearned fees paid for referrals by companies such as lenders, insurance companies, escrow companies, and title companies.

7. **B** The borrower must receive the Loan Estimate within three days of submitting an application. The Closing Disclosure must be given to the borrower no later than three days before consummation of the loan.

8. **B** A mortgage broker can loan his own funds if the borrower is informed of the source of funds.

9. **A** It requires reporting and recordation of those who make, arrange, or service loans secured by real property.

## Multiple-Choice Questions

1. **B** One discount point is 1% of the loan amount. Lenders, a.k.a. loan originators, charge discount points because it increases the lender's upfront profit or yield. Note: Borrowers pay discount points because, when they do, lenders lower the interest rate on the loan. The other answers are incorrect: A discount point is typically paid by a borrower, but it can also be paid by, for example, an employer or a motivated seller. Paying a discount point or two can save a borrower a great deal of money. However, it is much less financially advantageous for the borrower if the loan is refinanced or the property is sold during the term of the loan.
2. **A** The buyer most likely got the VA fully guaranteed home loan. Provided all qualifications are met, this type of financing is available not only to veterans, but also to the widows or widowers of veterans. Because this is fully guaranteed by the VA, eligible borrowers are typically not required to put a down payment on the subject property. In contrast, under the FHA home loan program, borrowers are required to make a small down payment. Currently, the minimum down payment for an FHA home loan is 3.5%. The fact that the buyer received a deed from the seller at the close of escrow indicated that the type of financing was not through the CalVet home loan program. For this state-level program, the government uses a land contract, meaning that the buyer will not receive a deed until the land contract is paid in full. A conventional home loan is neither insured nor guaranteed by the government. Nearly every buyer getting a conventional home loan will be required to make a down payment. Traditionally, with a conventional home loan for a purchase money mortgage, the down payment was 20% of either the purchase price or the appraised value, whatever was less.

3. **A** A deed of trust, signed by the borrower, is a financing instrument that pledges realty as collateral for the loan. The only word from these choices that means borrower is "mortgagor." In fact, the borrower is called a "trustor" on the deed of trust. "Mortgagee" (on a mortgage) and "beneficiary" (on a deed of trust) are terms for the lender. The holder of a nonfreehold estate is a tenant: The question states it was the owner of the property who took out the loan.

## Laws of Agency and Fiduciary Duties

### True/False Questions

1. **A** Compensation is not a requirement of an agency relationship.
2. **A** The broker of record is the agent and the one employed to represent principals.
3. **B** The agreement does not have to be in writing, unless the law requires a writing or the agent is to perform an act on behalf of the principal that requires a writing.
4. **A** An agency could also be established by a subsequent ratification by a principal of an activity of the agent that held out an agency relationship.
5. **A** The real estate agent owes the principal the following duties of a fiduciary: obedience, loyalty, disclosure, confidentiality, accounting, and reasonable care and skill.
6. **B** The duty of loyalty states that an agent's interests must be subordinated to their client's.
7. **A** The agent must make an accounting to the principal of the details of the transaction.
8. **B** Representation must be disclosed before contractual obligation.
9. **B** When representing both the buyer and the seller, the agent must get consent of both parties in writing.
10. **B** A salesperson may represent herself with proper disclosure to the other party.

11. **A** Working with a relative or any person with whom the agent has a significant relationship must be disclosed in writing.

12. **B** The broker is the agent in the relationship, not the salesperson. Death of either the principal or the broker will terminate an agency.

13. **B** The principal or agent always has the power to terminate the agency unilaterally.

14. **B** The commission is earned when the real estate broker finds a buyer who is ready, willing, and able to purchase the subject property on the seller's original terms, or when the seller accepts a purchase offer at agreed-on terms.

15. **A** In other words, the agent must be the person who initiated the contact that brought the third party to the principal.

16. **B** A real estate agent owes to a third person a duty of full disclosure of material facts.

17. **A** The State of California does not consider this a material fact.

2. **D** Preprinting a commission rate in the listing agreement violates federal antitrust laws. The other choices are legal. It is lawful for a real estate broker to limit professional activity to a familiar geographic area (a.k.a. a "farm"): However, it would be a violation of antitrust laws to carve up territories with other brokers. It is also lawful for a successful broker to refuse to accept anything less than a certain commission rate, provided that the prospective seller was informed that commissions are generally negotiable. Finally, most brokers in California refuse to accept anything other than the exclusive right-to-sell listing agreement, and it is legal to do so.

3. **A** If the listing agent owes a fiduciary duty to a client, the associate licensee owes that client the same fiduciary duty. Because the listing broker owed the seller the fiduciary duty of confidentiality, the salesperson did as well. The other answers are incorrect: All material facts *about the subject property* (not about the principal) must be disclosed to all interested parties to a transaction. Unless there is a dual agency, the listing agent (the seller's agent) will not owe fiduciary duties to the buyer. Note: The salesperson and the seller are not in an agency relationship with each other. Nevertheless, the salesperson is in an agent of the employing broker and must obey the laws of agency regarding the employing broker's clients.

## Multiple-Choice Questions

1. **B** If a party permits the false appearance of agency when an agency relationship does not exist, and an innocent third party is thereby misled into believing an agency relationship exists, the party that created the misapprehension of agency may face a future legal penalty. That legal penalty will include being "estopped" or prevented from testifying in court that, at the time the innocent third party was being misled, there was no agency relationship. *Agency by estoppel* and *ostensible agency* are synonyms. *Agency by conversion prevention* is a made-up term.

## Practice of Real Estate and Disclosures (Includes Specialty Areas)

### True/False Questions

1. **A** This money would be used to cover bank account fees.

2. **B** The purpose is to keep a broker's funds separate from the broker's clients. Commingling is the illegal act of mixing the licensee's own money with the money held for others.

3. **A** It is an act prohibited by the Civil Rights Act of 1968.

4. **A** The prohibition applies to all loans for the financing of dwellings of one to four units, including conventional, FHA-insured, and VA-guaranteed loans.

5. **A** Failure to disclose this fact and provide the name of the licensee is called blind advertising and is illegal.

6. **B** The legal requirement is removal within 48 hours after receipt of notice.

7. **A** Trust fund records must be kept for three years and must be open for inspection by the real estate commissioner.

8. **B** Brokers are responsible for supervising all salespersons and broker associates.

9. **B** They may, but the CMA is subject to the approval of, and for use by, the licensee.

10. **A** The commissioner must have been for 5 years a real estate broker active in California, or the commissioner must possess related experience associated with real estate activity in California for 5 years within the last 10 years.

11. **A** If the continuing education requirements are not met by the end of the four-year term, the license is canceled and the licensee has a two-year grace period to complete continuing education requirements, pay a late fee, and renew the license.

12. **A** Five are mandatory and three are electives.

13. **A** There is also a maximum of \$250,000 per licensee that can be paid.

14. **B** The license is suspended, and reinstatement cannot be considered until the licensee has fully reimbursed the fund for the amount paid out plus interest.

15. **A** It is an excellent guide to ethical behavior.

16. **A** The educational requirements for certification will prepare licensees for more effective online communication.

17. **B** A resident manager lives on the property and does not require a license.

18. **B** In a gross lease, the tenant pays rent and the landlord pays all expenses. In a net lease, the tenant pays some or all of the property's expenses (property taxes, hazard insurance, and maintenance costs).

19. **A** In a time-share project, a purchaser receives the right to exclusive use of a portion of the property for a particular period of time each year.

20. **A** The seller of residential property of one to four units must provide the buyer with a written TDS.

21. **A** The Natural Hazards Disclosure Statement meets this and other requirements.

22. **A** The disclosure laws impose obligations not only on real estate licensees but also on the principals to the transaction.

23. **A** There are no exceptions to or exemptions from this law.

24. **A** The purchasers must sign that they received and accepted the report before they are bound to complete the purchase.

25. **A** Real estate agents must recognize our rapidly changing national demographics.

### Multiple-Choice Questions

1. **C** These classes are protected under California fair housing laws. Here are the classes protected under federal fair housing laws: race, religion, color, national origin, sex (added in 1974), family status (added in 1988), and handicap/disability (added in 1988).

2. **A** A “blind advertisement” is one that does not disclose that a real estate licensee is involved in the transaction. Both California statutory law and DRE regulations require advertising materials intended to be first point of contact with the public show real estate licensure and the licensee’s eight-digit real estate license number. The advertisement described in the fact pattern is considered the first point of contact, and it must comply with the rules related to blind advertising. Mortgage loan originators (MLOs), including real estate brokers engaged in loan brokerage activities, are also legally prohibited from engaging in blind advertising. Blind advertising is illegal, even if the subject property is subject to governmental regulations such as those imposed by the California Coastal Commission.

3. **A** Provided all DRE requirements are met, a broker of record may delegate the responsibility to supervise associate licensees to a branch or a division manager. This delegation makes both the broker of record and the branch or division manager liable for the actions of associate licensees. The appointment must be in a written contract, and the DRE must be informed of the delegated responsibility. The branch or division manager cannot hold a restricted license or be subject to an order of debarment. Real estate salespeople can serve in this position, provided that, prior to the appointment, they have two years of full-time real estate experience in the preceding five years.

4. **D** An attorney-at-law who works as a real estate agent with any type of real estate—commercial or otherwise—must have an active and valid real estate license issued by the DRE. The other choices are exemptions from California real estate licensing requirements. Note: An attorney-in-fact under a power of attorney is an agent acting in place of a principal and is, therefore, not required to have a real estate license.

5. **D** Puffing is an exaggerated form of sales talk that no reasonable person will rely upon to make a decision. A good way to test if something is either a misrepresentation (a lie) or puffing is to check if the statement can be measured objectively. Here, it would be impossible to objectively determine if the house is “fantastic” or has “the most beautiful view of the city.” These are subjective opinions that can’t be measured objectively. Puffing is not illegal. Here, however, puffing is unethical because the listing agent does not believe these statements to be true. Ethical behavior is about what is moral, right, and just. Duress is the illegal use of force: There is no suggestion in the fact pattern that the real estate broker used force. Note: Local district attorneys and the DRE only investigate illegal activities, not unethical activities.

6. **B** In order to finance the purchase of a manufactured home with a traditional mortgage, major institutional lenders require that the manufactured home be permanently affixed to the real estate. A manufactured home built in the U.S. after June 1976 must be constructed according to federal Housing and Urban Development (HUD) building codes. Therefore, provided that the manufactured home is permanently affixed to the realty, HUD’s building codes will not prevent the client from financing the purchase with a traditional mortgage. The other answer choices all indicate that the manufactured home is not permanently affixed to the real estate. An affidavit of affixture is a recordable document executed by a local government official who has inspected the manufactured home to verify it has been permanently affixed to the real estate. A manufactured home registered with the California Department of Housing and Community Development (HCD) is unaffixed to real estate, meaning it is personal property. Finally, if a manufactured home is still equipped to be transported on a highway, that indicates it is not permanently affixed to real estate. Note: A manufactured home was previously known as a “mobile home.”

7. **D** None of these reports is legally required for the purchase of a one-to-four-unit residential dwelling. The preliminary report of title insurance is issued by title insurance companies prior to the issuance of the policy. It is an offer to insure based on the conditions in the report and the payment of a one-time title insurance policy premium. Sellers frequently buy buyers a standard (CLTA) owner's policy of title insurance, but it is not a legal requirement. Lenders may condition financing on the purchase of an extended (ALTA) lender's policy of title insurance. Lenders typically make the borrowers pay for this policy. However, that is a lender's financing condition, not a legal requirement. A pest control report is another common loan condition but not a legal requirement. A home inspection is not legally required.

11. **B** A certified residential license allows an appraiser to appraise nonresidential property up to a transaction value of \$250,000. Only an appraiser with a certified general license can do appraisals of all real estate.

12. **A** The goal of the analysis is to select the value that is most likely to be an accurate reflection of market value.

13. **B** It fails to take into account the many variables that contribute to gross income.

14. **A** The cap rate can be expressed as the relationship between the net operating income the property produces and its market value. The equation is net operating income divided by value equals cap rate.

## Property Valuation and Financial Analysis

### True/False Questions

1. **B** An appraisal is an estimate of the market value as of a specified date.

2. **B** Market value is objective, because it is not based on the requirements of a particular buyer.

3. **A** Real estate is described as having a value in use, which refers to its value when used for a particular purpose.

4. **B** Cost is not an element of value.

5. **A** Demand, utility, scarcity, and transferability.

6. **A** Comparison, cost, capitalization

7. **B** The cost approach requires building cost data.

8. **A** This method is usually the most significant in appraising residential property.

9. **B** The sales price adjustments are made to the comparables to more accurately reflect the features of the subject property.

10. **A** Using the square-foot method, the appraiser multiplies the current cost per square foot of a comparable building by the number of square feet in the subject building.

### Multiple-Choice Questions

1. **A** Transferability is a basic element of value. Value is affected when there is something impeding the timely sale of a property. Both answer choices here might delay the transfer of the property on the north side of the street and would be causes for the appraiser's lower estimate of value. Note: The other three elements of value are demand, utility, and scarcity.

2. **D** During the reconciliation process of an appraisal, the appraiser will weigh estimates of value from all three approaches (market data, cost, and income) before arriving at a final opinion of value. The final estimate of value is not an average of these three methods. Given the historic nature and location of the subject property, the appraiser would likely rely upon the cost approach. However, this test question focuses upon the final reconciliation (or correlation) phase of the appraisal. During this process, the appraiser considers the market data, the cost, and the income approach before choosing an estimate or opinion of value that relies upon the method most appropriate for the property being appraised.

## Transfer of Property

### True/False Questions

1. **A** It provides a more thorough coverage than that provided in a standard policy.
2. **B** The grant deed conveys after-acquired title. A quitclaim deed is commonly used to clear a cloud on title.
3. **B** In this situation, a gift deed would be used. A reconveyance deed is given by the trustee to someone who has just paid off a home loan.
4. **A** Strict requirements must be met including, the broker must be the selling or listing broker in the transaction or a party to the transaction.
5. **A** The first installment, covering July 1 to December 31, is due November 1. The second installment, covering January 1 to June 30, is due February 1.
6. **B** For a deed to be valid, it only requires the signature of the grantor.
7. **A** The property is divided, if possible, or sold. After a sale, the court divides the proceeds according to the owners' shares.
8. **A** As long as the joint tenancy exists, the right of survivorship in the other joint tenants takes precedence over a will of the deceased joint tenant.

### Multiple-Choice Questions

1. **D** The subject of this test question is the legal doctrine of "after-acquired title." This legal doctrine specifically relates to a situation where a transferor—who is not the legal owner of real estate—attempts to transfer the property to a transferee. Then, later, the transferor becomes the owner of the property. The question is: Who owns the property when the transferor finally acquires title? There are circumstances when the acquisition of the property at a subsequent time will result in an automatic transfer to the transferee. If Mark O'Brien attempted to transfer the property to Bradford using a grant deed, then, when Mark O'Brien acquired the property, it would automatically (through operation of law) transfer to Benjamin Bradford. The other answers are incorrect: A quitclaim deed transfers whatever interest the transferor has in the property at the time of the conveyance. Here, at the time of the conveyance, Mark O'Brien held no ownership interest in the property. A trust deed is a financing instrument used when someone is taking out a loan. This loan document would not be used to convey title to a condo unit. A trustee's deed (a.k.a. a "trustee's deed upon sale") is used at a foreclosure: It conveys the property from the trustee under a deed of trust to the winner of the foreclosure sale.
2. **D** The buyer will not be credited—but will be debited—for the prepaid property taxes. It's the seller who would be credited for the 1½ months (45 days) of prepaid property taxes. Note: Because the test question states that this is being calculated using the "30/360-day count convention for proration calculations," each month has 30 days and a year has 360 days. Thus, 1½ months is 45 days.

3. **B** The foreclosure described in the test question is the nonjudicial foreclosure. The two required notices are the Notice of Default and the Notice of Sale. Twenty days after the Notice of Sale records, the property can legally be sold and is conveyed by the trustee to the new owner with a deed called the Trustee's Deed upon Sale (a.k.a. a "Trustee's Deed"). In California, the nonjudicial foreclosure process is overwhelmingly used when borrowers default on their loans. Why? A nonjudicial foreclosure is faster and less expensive for the lender than a judicial foreclosure. The other answers are incorrect: A deed of reconveyance is the document executed by the trustee when the loan is paid in full: It releases the lien from the property and reconveys bare legal title back to the owner of the property. Respondeat superior is a legal doctrine related to agency relationships: Per this doctrine, the principal will be held legally and financially responsible for the acts of the agent, provided those actions were within the scope of the agent's authority. Lis pendens means "lawsuit pending." When recorded, this document provides constructive notice ("notice to all the world") that there is a lawsuit pending on a specific property. A certificate of sale is given to the winner of a foreclosure sale at a judicial foreclosure: The test question states that this was a nonjudicial foreclosure. Constructive notice is notice implied by law to all the world when a document is recorded. This compares to actual notice, which is direct knowledge. Neither constructive notice nor actual notice is a recordable document. A lieu deed is a deed in lieu of foreclosure. This is the deed a borrower gives to the lender to avoid foreclosure.

4. **C** Because this owner was incapacitated and had not executed a power of attorney, the California probate court would likely have appointed a conservator to sign legal documents such as a deed. The probate court supervises conservators and must approve activities such as the sale of the owner's real estate. The other answers are incorrect: An attorney-in-fact is an agent appointed under a POA, a legal document the test question stated the owner had not executed. An implied agency relationship is created accidentally or unintentionally by the implied agent. Per the test question, the owner was not in any agency relationship prior to the car accident. Finally, an escrow officer is a dual agent, neutrally serving both the buyer and the seller. An escrow officer would not have the authority to sign a document like the seller's deed.

